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Decision 00-03-021 March 2, 2000

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Joint Application of GTE Corporation ("GTE") and Bell Atlantic Corporation ("Bell Atlantic") to Transfer Control of GTE's California Utility Subsidiaries to Bell Atlantic, Which Will Occur Indirectly as a Result of GTE's Merger with Bell Atlantic.	Application 98-12-005 (Filed December 2, 1998)

(See Attachment A for list of appearances.)

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OPINION

1. SUMMARY

Pursuant to California Public Utilities Code §§ 852 and 854, GTE Corporation and Bell Atlantic Corporation seek approval to transfer GTE's California utility subsidiaries to Bell Atlantic, which will occur as a result of the merger of GTE with Bell Atlantic. Before authorizing the merger, we must find that the proposed merger provides economic benefits to ratepayers; equitably allocates those benefits, with ratepayers receiving no less than 50% of the benefits; does not adversely affect competition; and is, on balance, in the public interest. We may adopt conditions, if necessary, to ensure that the proposed merger does not adversely affect competition and is in the public interest. We approve the application with limited conditions and clarifications.

We find that the proposed merger provides economic benefits of $168.1 million (net present value) over five years. We allocate 50%, or $84.1 million (net present value) to ratepayers. The ratepayer share will be distributed in the form of $64.3 million (net present value) in surcredits, and $19.8 million (net present value) to fund provisions of the Community Collaborative Agreement. The initial surcredit will be about 0.950%, or about $0.32 per month on the average residential bill, and $0.47 per month on the average business bill. The surcredit will be adjusted annually to reflect changes in the billing base.

We find that the merger will not adversely affect competition. We adopt conditions and clarifications with our approval of the merger relating to the total amount of benefits allocated to ratepayers, distribution of those benefits by both a surcredit and funding of the Community Collaborative Agreement, approval of funding for the Community Collaborative Agreement, preparation of service quality monitoring reports, and sharing of state-level accounting cost information.

We conclude that the proposed merger is, with these limited conditions and clarifications, on balance in the public interest. The proceeding is closed.

2. BACKGROUND

GTE Corporation (GTE) and Bell Atlantic Corporation (Bell Atlantic; collectively applicants) seek approval to merge, pursuant to California Public Utilities Code §§ 852 and 854.[1]

2.1. Description of Applicants and Proposed Merger

2.1.1. GTE

GTE is a New York corporation headquartered in Irving, Texas. It is a diversified telecommunications holding company with subsidiaries providing a wide variety of communications services in the United States and several foreign countries.[2] Those services include voice, video and data transport; network access; wireless communications; directory publishing; advertising; internet access; web-hosting; paging; and public telephones. GTE has domestic local telephone operations in 28 states,[3] with approximately 23.5 million access lines, and four million wireless customers.

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[1] All statutory references are to the California Public Utilities Code unless stated otherwise.

[2] GTE provides telephone access service in the United States, Canada, the Dominican Republic, and Venezuela. GTE provides wireless service in the United States, Canada, the Dominican Republic, Argentina, Venezuela and Taiwan. GTE participates in a paging network venture in China.

[3] Those states are: Alabama, Alaska, Arizona, Arkansas, California, Florida, Hawaii, Idaho, Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, Missouri, Nebraska, Nevada, New Mexico, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, Texas, Virginia, Washington, and Wisconsin.

There are 11 GTE subsidiaries operating in California, regulated in whole or part by this Commission as public utilities:

1. GTE California Incorporated (GTE California; U 1002 C);
2. GTE West Coast Incorporated (U 1020 C);
3. GTE Communications Corporation (formerly known as GTE Card Services, d.b.a. GTE Long Distance; here referred to as GTECC; U 5494 C);
4. GTE Mobilnet of California Limited Partnership (U 3002 C, U 4038 C);
5. GTE Mobilnet of Santa Barbara Limited Partnership (U 3011 C, U 5145 C);
6. GTE Mobilnet of San Diego Incorporated (U 3048 C, U 5689 C);
7. GTE Mobilnet of Central California Incorporated (U 3030 C, U 3035 C);
8. Fresno MSA Limited Partnership (U 3005 C);
9. California RSA No. 4 Limited Partnership (U 3038 C);
10. GTE Mobilnet of California, Inc. (U 5582 C); and
11. GTE Telecommunication Services Incorporated (U 5495 C).

GTE California and GTE West Coast are incumbent local exchange carriers (ILECs). GTE California serves approximately 4.6 million access lines in California. GTECC is licensed to provide competitive local exchange service and long distance service in California. GTE Wireless Incorporated provides wireless services through various GTE Mobilnet entities, including in California.

2.1.2. Bell Atlantic

Bell Atlantic is a Delaware corporation headquartered in New York, New York. It is a diversified telecommunications holding company, the subsidiaries of which provide voice and data transport and calling services; network access; wireless services; directory publishing; and public telephones.

Bell Atlantic is one of the Regional Bell Operating Companies (RBOCs) created in 1984 with the divestiture by the American Telephone and Telegraph Company of its local telephone operations. In 1997, Bell Atlantic merged with NYNEX, another Regional Bell Operating Company.

Bell Atlantic's local telephone operating companies provide services in 14 jurisdictions within the Northeast and Mid-Atlantic states and the District of Columbia. It has approximately 41 million domestic access lines and more than six million domestic wireless customers, and has operations and investments in 21 foreign countries.[4]

Bell Atlantic has two subsidiaries regulated in whole or part by this Commission as public utilities:

1. Bell Atlantic Communications, Inc. (U 5732 C); and
2. NYNEX Long Distance (d.b.a. Bell Atlantic Long Distance; U 5658 C).

As of June 1999, these two subsidiaries served approximately 440 long distance customers on a resale basis in California.

2.1.3. Proposed Merger

GTE and Bell Atlantic executed an Agreement and Plan of Merger on July 27, 1998. The proposed transaction involves a merger of GTE and Bell Atlantic, the parent holding companies. The Merger Agreement provides for Beta Gamma Corporation, a wholly owned subsidiary of Bell Atlantic, to merge with and into GTE. As a result, GTE will continue as the surviving corporation and become a wholly owned subsidiary of Bell Atlantic, with GTE's California utility subsidiaries becoming second-level subsidiaries of Bell Atlantic.

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[4] Bell Atlantic's foreign operations include Latin America, Europe, Asia, and the Pacific Rim.

The Merger Agreement provides for a tax-free stock-for-stock exchange. At the effective date of the merger, each outstanding share of GTE common stock will be canceled and converted into the right to receive 1.22 shares of common stock of Bell Atlantic.

According to applicants, this is a "merger of equals," with GTE and Bell Atlantic sharing evenly in the management responsibility for the merged company. Prior to closing, the respective boards of directors of GTE and Bell Atlantic will each select half of the board of directors of the combined company, to the extent possible from current directors of the respective companies. The Merger Agreement also provides that the bylaws of the combined company will be amended to ensure that the combined company's board of directors (and each committee thereof) will continue to have an equal number of directors designated by GTE and Bell Atlantic until July 1, 2002. GTE Chairman Charles R. Lee will become Chairman of the combined company. Lee will also serve as Co-Chief Executive Officer of the combined company, together with Bell Atlantic Vice Chairman and Chief Executive Officer Ivan Seidenberg. Seidenberg will become the sole Chief Executive Officer on July 1, 2002. Lee will continue to serve as Chairman until June 30, 2004, when he will be succeeded by Seidenberg. The combined company will be incorporated in Delaware, and headquartered in New York City.

Applicants state that the transaction does not involve an operational consolidation of any local telephone operating companies. Further, applicants say that GTE's California utility subsidiaries will continue to provide services under the same terms, conditions and regulations that apply prior to the merger, except for the rate reductions that will result from § 854(b)(2).[5] No operations, lines, plant, franchises or permits of regulated subsidiaries will be merged with the lines, plant, franchises or permits of any other regulated public utility, according to applicants. Applicants assert that such changes, if any, which may be made at a later date will only be made subject to such approvals as required by the Public Utilities Code and the Commission.

2.2. Procedural Background

The joint application was filed on December 2, 1998. Timely protests and responses were filed on January 15, 1999. A prehearing conference (PHC) was held on February 2, 1999. The Scoping Memo and Ruling of the Assigned Commissioner was filed and served on February 16, 1999, wherein the issues and schedule were stated, the proceeding was categorized as ratesetting, and Administrative Law Judge Burton W. Mattson was designated the Principal Hearing Officer and Presiding Officer.

On April 1, 1999, in consultation with the Assigned Commissioner, the Presiding Officer preliminarily ruled that the following groups are eligible to seek compensation for participation in this proceeding:

The Utility Reform Network (TURN)
Greenlining Institute (Greenlining)
Latino Issues Forum (LIF)
National Council of La Raza
Southern Christian Leadership Conference
Filipinos for Affirmative Action
Filipino Civil Rights Advocates
Korean Youth and Community Center
California Rural Indian Health Board
Association of Mexican American Educators

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[5] Section 854(b)(2) provides that ratepayers shall receive no less than 50% of the economic benefits of the merger.

California Association of Asian-Pacific Bilingual Education
(These latter eight groups, plus the California Association for Bilingual Education discussed below, are referred to herein as Public Advocates.)

By ruling dated April 23, 1999, the schedule was delayed about one month to allow for additional discovery. Discovery disputes were resolved by rulings issued in March, May, and June 1999. By ruling dated June 1, 1999, a motion to dismiss the joint application was taken under submission, and an alternate motion to suspend the schedule was denied.

Proposed testimony and proposed rebuttal testimony were served in June 1999. A second PHC was held on July 6, 1999. Thirteen days of evidentiary hearings were held between July 12, 1999 and July 28, 1999, during which 146 exhibits were received and 1,832 pages of hearing transcripts taken.[6] Opening briefs were filed on August 27, 1999.

On August 31, 1999, in consultation with the Assigned Commissioner, the Presiding Officer preliminarily ruled that the California Association for Bilingual Education is eligible to seek compensation for participation in this proceeding. Pursuant to § 854(b)(3), on September 15, 1999, the California Attorney General filed an Opinion on the competitive effects of the proposed merger. On September 24, 1999, parties filed reply briefs, and the matter was submitted for decision. On October 5, 1999, parties filed an issue matrix summarizing the issues and their positions.

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[6] On August 17, 1999, applicants moved to unseal certain exhibits and portions of other exhibits. The motion was granted by ruling dated August 23, 1999. Applicants were directed to serve an amended version of each exhibit wherein a portion would be unsealed, with a proposed exhibit number, by September 10, 1999. On September 10, 1999, applicants served 13 proposed exhibits with proposed exhibit numbers. No party has stated any comment or objection. The proposed exhibit numbers are adopted, and each proposed exhibit with portions unsealed is received effective September 10, 1999.

By ruling dated December 10, 1999, the motion to dismiss was denied. On December 22, 1999, the proposed decision (PD) of the Principal Hearing Officer was filed and served. Timely comments were filed on January 11, 2000, and reply comments on January 18, 2000. We incorporate herein comments and reply comments that we find reasonable. We complement parties for generally well-written and well-documented briefs, reply briefs, comments and reply comments. It is refreshing to have such good material for our consideration.

2.3. Status of Proposed Merger

The United States Department of Justice (DOJ) reviewed the merger for violation of federal antitrust laws. On May 7, 1999, the DOJ agreed not to challenge any aspect of the proposed merger, subject to applicants agreeing to divest their interests in overlapping wireless territories in 65 markets located in nine states, none of which are in California. Applicants have agreed to this condition.

The shareholders of GTE approved the merger on May 18, 1999. The shareholders of Bell Atlantic approved the merger on May 19, 1999.

2.4. Timeliness of Decision

This decision is timely. It is issued well before the 18-month time period set forth in Senate Bill 960, Section 1 (Ch.856, Stats.1996).

2.5. Burden of Proof

Applicants must prove by a preponderance of the evidence that the proposed merger meets the requirements for approval. (§ 854(e).) In particular, applicants must prove that the proposed merger provides short-term and long-term economic benefits to ratepayers, does not adversely affect competition, and is in the public interest. (§§ 854(b) and (c).)

Preponderance of the evidence:

"means that evidence in support of Applicants' position, when weighed with that opposed to it, must have the more convincing force and the greater probability of truth. (1 Witkin, California Evidence (3d. Ed. 1986) § 157, and cases cited thereunder.)

"Black's Law Dictionary defines 'preponderance' as 'greater weight of evidence, or evidence which is more credible and convincing to the mind[;t]hat which best accords with reason and probability.'" (Decision (D.) 91-05-028, 40 CPUC2d 159, 172.)

Said differently,

"[t]he preponderance standard is one that asks which outcome is 'more likely than not.' Leslie G. v. Perry & Associates et al., (1996) 43 Cal. App. 4th, 472, 489." (Applicants' Reply Brief, p. 58.)

3. ECONOMIC BENEFITS

The Public Utilities Code requires that:

"Before authorizing the merger, acquisition, or control of any...telephone utility organized and doing business in this state...the commission shall find that the proposal does all of the following:

(1) Provides short-term and long-term economic benefits to ratepayers.

(2) Equitably allocates, where the commission has ratemaking authority, the total short-term and long-term forecasted economic benefits, as determined by the commission, of the proposed merger, acquisition, or control, between shareholders and ratepayers. Ratepayers shall receive not less than 50 percent of those benefits." (§ 854(b).)

3.1. Economic Benefits for Ratepayers

Applicants argue that their proposal will provide ratepayers with direct economic benefits of $55.9 million (net present value, or NPV).[7] In addition, applicants contend that ratepayers will enjoy cost savings attributable to competitive and unregulated services that will be passed through to consumers by

[7] Applicants calculate benefits over four years.

competitive forces, along with innovative products and services that may be offered as a result of the merger.

The Office of Ratepayer Advocates (ORA) estimates ratepayer economic benefits of at least $466 million (NPV),[8] while TURN estimates ratepayer benefits of at least $557.6 million (NPV).[9] Public Advocates, Greenlining and LIF contend that, in addition to benefits arising from competition and innovative products and services, the Community Collaborative Agreement (CCA)[10] provides both short- and long-term economic benefits to all ratepayers, including the most under-served.

Only AT&T Communications of California, Inc. (AT&T), MCI WorldCom, Inc. (MCI), and Sprint Communications Company L.P. (Sprint) contend that there may not be economic benefits for ratepayers. AT&T, MCI and Sprint argue that applicants have provided insufficient information and analysis to assess the economic benefits. Based on this and other grounds, on May 26, 1999, these parties moved for dismissal of the application.

We are not persuaded by AT&T, MCI, and Sprint that there may not be economic benefits for ratepayers. For all the reasons explained below, we find applicants have met their burden of proof. We affirm the December 10, 1999 ruling of the Presiding Officer denying the motion to dismiss.

Applicants estimate that the proposed merger has a benefit-to-cost ratio of 2.6, with a 90% probability that the ratio is between 2.2 and 2.9. No party presents

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[8] ORA Opening Brief, Table 1. ORA calculates benefits over eight years.

[9] TURN Opening Brief, p. 4. TURN calculates benefits over 10 years; $557.6 million is the NPV equivalent of $83.9 million per year for 10 years at a 10.5% discount rate.

[10] The CCA is an agreement between applicants and many public interest and community groups. It generally seeks to provide increased telecommunications access in otherwise under-served communities, and is discussed in detail later in this decision.

any specific estimate to the contrary. No party argues that less than 50% of those benefits should be allocated to ratepayers. No party presenting specific evidence on benefits estimates those benefits to be less than applicants' proposed composite short-term and long-term $55.9 million (NPV) to ratepayers.

Therefore, we are convinced there are short-term and long-term economic benefits for ratepayers. Those direct benefits are at least $55.9 million, and may be more. They also include benefits from competition, enhanced growth opportunities, and the leveraged advantages provided by the CCA, all of which we discuss below.

3.2. Amount of Economic Benefits

3.2.1. Applicants' Estimate

Applicants' proposal was developed by:

(1) estimating the total amount of expense and capital synergies that GTE and Bell Atlantic jointly expect to achieve across all of their operations (which they estimate to be $2 billion in expense synergies, and $500 million in capital synergies),

(2) allocating the aggregate estimate between GTE and Bell Atlantic,

(3) determining the total amount of net savings attributable to GTE by offsetting merger-related costs,

(4) determining the portion of GTE savings attributable to GTE California, and

(5) determining the portion of GTE California savings attributable to its intrastate Category I and Category II services.

Applicants then developed the net present value of the resulting estimate using four years as the long term. Their result is $111.7 million. Applicants propose allocating 50%, or $55.9 million, to ratepayers through an annual surcredit of $10.4 million applied to the CHCF-B billing base for four years, and through funding of the CCA.

Parties accept many aspects of applicants' benefit and cost development. For example, no party presents any specific alternative to applicants' proposal that the economic benefits accruing to GTE California's Category I and II services are the only benefits that need to be allocated to ratepayers through an explicit flow-through mechanism. No party challenges applicants' estimate of transaction and implementation costs, or proposes to exclude any of applicants' estimated costs (although ORA recommends a different allocation). No party takes issue with, or proposes specific alternatives to, applicants' NPV methodology, the discount rate, the use of a levelized surcredit, the allocation factors used to allocate GTE-wide savings to GTE California's intrastate Category I and II services, or the proposed 50-50 allocation of benefits between ratepayers and shareholders.

Nonetheless, parties propose several adjustments. Those include whether applicants' estimate should be adjusted for the actual experience of other mergers, whether $600 million of additional savings from best practices should be included, how expense savings should be allocated, how transaction and implementation costs should be allocated, whether costs should be expensed or amortized over the life of merger benefits, whether revenue increases resulting from the merger should be included in benefits, and what should be the period for calculating short-term and long-term economic benefits. As a result, ORA asserts that total economic benefits are $932.0 million (NPV), and TURN says they are $1,115.2 million, compared to applicants' estimate of $111.7 million.[11]

While we accept some adjustments, and reject others, applicants have met their burden of proof, and we adopt applicants' estimates unless discussed below. (See Attachment B.) Applicants' estimates were developed by senior

[11] Since economic benefits allocated to ratepayers are 50% of total economic benefits, total economic benefits are twice the ratepayer benefits referenced earlier herein.

executives from both companies with extensive knowledge of, and experience with, each company's budgets and operations. The estimates were prepared using a collaborative process that became known as the August 21 Group.[12] Some of the executives involved had previous experience in estimating and tracking merger savings, making them particularly well qualified to develop the savings estimate here.[13]

Further, as discussed below, applicants' estimate is supported by comparisons with other mergers. Moreover, if it errs, it errs in favor of ratepayers. For example, applicants do not propose an adjustment to reflect GTE's early 1999 workforce reduction program (which will eliminate 9,000 employees included in GTE's planned expenses at the time applicants estimated merger savings, making achievement of the merger savings more difficult).

In addition, applicants' estimate was developed for presentation to diverse groups, including shareholders, employees and the investment community. Applicants had an incentive to neither understate, nor overstate, their estimate.

3.2.2. Experience With Other Mergers

Applicants compared their estimates of costs and savings to those estimated for other utility mergers. Applicants show that, as a percentage of each company's combined expense base, the GTE and Bell Atlantic estimates are in line with the savings estimated in the mergers of SBC Communications, Inc./Pacific Telesis Group (SBC/Telesis) and SBC/Ameritech. Applicants also compared the general and administrative (G&A) savings estimated in various electric utility

[12] August 21, 1998.

[13] That experience included the Bell Atlantic/NYNEX merger, and the GTE/Contel merger.

mergers to the G&A savings estimated by applicants, and show that applicants' estimate, as a percentage of their combined operating expenses, is in line with estimates for nine electric utility mergers.

TURN argues that applicants' savings estimate understates the amount of savings applicants will likely achieve, and recommends that applicants' savings estimate be increased by 50%. TURN bases this recommendation on its study of pre-merger estimates of savings versus actual, or updated, savings from other mergers, including Bell Atlantic/NYNEX, SBC/Telesis, and SBC/Ameritech. We decline to adopt TURN's recommendation.

TURN's proposed adjustment assumes that the same alleged understatement of savings for the Bell Atlantic/NYNEX merger is likely to have occurred for the GTE/Bell Atlantic merger because some of the same people were involved in analyzing both mergers. To the contrary, the record here shows that the Bell Atlantic/NYNEX merger proved to be a useful learning experience for those involved. The experience gained in estimating and achieving the savings from the Bell Atlantic/NYNEX merger makes applicants' estimate here more, not less, reliable.

Moreover, TURN's rationale ignores the contribution made by GTE personnel. For example, Bell Atlantic's initial pre-merger estimate of expense savings was revised upward by $700 million (from $1.3 billion to $2.0 billion) based on input from GTE's Shuell, and others, in the August 21 Group.

TURN argues that Bell Atlantic continued to underestimate, as demonstrated by its initial estimate of $1.3 billion. We think otherwise. The timing of the mergers and studies discussed below, as well as the fact that Bell Atlantic executives agreed to increase the estimate here to $2.0 billion, show us that the August 21 Group had the opportunity to take advantage of experience, and did so.

For example, the updated estimates from the Bell Atlantic/NYNEX and SBC/Telesis mergers were available and formed one of the bases of the work performed by GTE's Shuell and the August 21 Group, as applicants' witnesses testified. Moreover, the presentation made by SBC and Ameritech to investment analysts at the time of their merger announcement (cited by TURN in support of its proposal) was specifically considered by Shuell and produced to TURN in response to a request for workpapers relating to Shuell's analysis.

In fact, the data show that applicants' savings estimate is consistent with revised estimates for the Bell Atlantic/NYNEX merger. As revised in 1997, Bell Atlantic and NYNEX expect to achieve \$1.1 billion in annual expense synergies and \$300 million in capital synergies by the year 2000, for a total of \$1.4 billion. In 1996 when they announced their merger, the combined operating expenses of Bell Atlantic and NYNEX were approximately \$23 billion. In the GTE/Bell Atlantic merger, the comparable figures are \$2.0 billion annual expense synergies, \$0.5 billion in capital synergies, for a total of \$2.5 billion in expense and capital synergies, with \$45 billion in combined operating expenses. The revised savings estimate for the Bell Atlantic/NYNEX merger is 6.1% of their then combined expenses.[14] That percentage compares to 5.6% for the GTE/Bell Atlantic merger.[15] Thus, applicants' estimate is in line with the revised estimate of savings, based on actual experience, from the Bell Atlantic/NYNEX merger.[16]

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[14] \$1.4 billion divided by \$23 billion equals 6.1%.

[15] \$2.5 billion divided by \$45 billion equals 5.6%.

[16] In contrast, TURN's recommended 50% adjustment would result in an estimate that would be 8.3% (\$2.5 B + (.50)(\$2.5B), divided by \$45 billion) of applicants' combined operating expenses.

Data from the Mercer Management Group (Mercer), an advisor hired by applicants to assess the benefits of the merger, show that the $2 billion estimated expense savings for the GTE/Bell Atlantic merger compares favorably to the estimated expense savings in other telecommunications mergers, even using revised estimates based on actual experience. (See Table 1.)

TABLE 1

Annual Expense Savings as a Percent of Expenses

Item	GTE - Bell Atlantic	SBC - Pacific Telesis	Bell Atlantic – NYNEX	SBC – Ameritech
Savings [a]	$ 2.0 billion	$1.2 billion	$1.1 billion	$1.6 billion
Percentage [b]	6.1 %	7.2 %	5.8 %	6.0 %

[a] Aggregate annual expense savings.

[b] Aggregate annual expense savings as a percentage of the combined entity's operating expenses before depreciation and amortization.

That is, the 6.1% for GTE/Bell Atlantic is in line with the 5.8% to 7.2% for other mergers, including updated data.

TURN argues that this data shows GTE/Bell Atlantic's estimate is too low. TURN contends that GTE is less efficient than other companies, and that the merger savings from the GTE/Bell Atlantic should, therefore, be greater. For example, TURN says that GTE/Bell Atlantic's estimate is $360.5 million too low if one simply applies the savings to expense ratio of SBC/Telesis.[17]

[17] TURN develops the $360.5 million as follows. GTE/Bell Atlantic's annual operating expenses are estimated to be $32.78 billion ($2.0 billion of savings divided by the savings to expense ratio of 6.1%). Increasing the savings to expense ratio by 1.1 percentage points (from 6.1% to 7.2%) increases savings by $360.5 million ($32.78 billion times .011). (TURN Reply Brief, p. 8.)

To the contrary, we reject the proposition that GTE is necessarily more inefficient that other companies. The cost data upon which TURN relies (e.g., expenses, expenses per access line) may measure efficiency, but this data also reflects other factors. For example, differences between companies (e.g., rural versus urban, relative age of plant, relative penetration of the latest technologies, relative mix of customers) can result in reasonable differences in costs. Without further information, one cannot reach TURN's conclusion.

Moreover, simply being the company with the lowest costs may not be desirable. No compelling data is presented here showing that the companies with the lowest costs are meeting customer needs, have high customer satisfaction rating, or are the best companies overall. Further, to the extent overall ratios provide a benchmark, the Bell Atlantic/NYNEX and SBC/Ameritech savings as a percent of expenses shown above supports the GTE/Bell Atlantic savings estimated here.

TURN cites the work of applicants' Merger Integration Teams to show that there are additional merger savings that should be included. We think otherwise. For example, in the area of "Telecom Network & Operation," the categories identified by the Merger Integration Teams overlap with those identified by GTE's Shuell. In a "Synergy Status Report," the synergies related to operator services are dependent on successful negotiation with unions. There is no reliable evidence upon which to determine or forecast the outcome of those negotiations.

The Merger Integration Teams are engaged in detailed analyses of savings opportunities. This does not indicate that applicants' overall estimate of expense savings is unreasonable or understated. To the contrary, the overall expense savings estimate of $2 billion is precisely the amount the Merger Integration Teams are relying on in their work and will seek to achieve as targets in planning the operations of the merged company.

TURN further justifies its proposed adjustment by noting that applicants' merger benefits forecast is still largely a work in progress, and that applicants have repeatedly stated that their estimates are preliminary. We agree that applicants' estimates represent a work in progress, and are largely preliminary. In fact, applicants adjusted their estimates for pension cost savings, and updated allocation factors, in response to the direct testimony of protestants. As updated, we believe applicants' estimates are the best information in this record (except for revenue increases and the definition of the long run, discussed below). We use the best information to reach the adopted level of benefits, and are not convinced by TURN that these estimates should be adjusted upward by 50%.

In further support of its recommendation to increase applicants' estimate by 50%, TURN cites an assertion by applicants' witness Landon that there is a 90% chance that actual savings are within 15% of applicants' estimate. TURN argues that this means there is a 90% chance that merger savings could be 15% higher than applicants' estimate of $2.5 billion (combined expense and capital savings), or an additional $375 million.

We are not convinced that this discredits applicants' estimate. The confidence interval also means that there is a 90% chance that the savings might be $375 million less than estimated by applicants.

TURN argues that applicants' citation to a range of benefits means applicants fail to satisfy the requirement of § 854, wherein TURN says ratepayers must be guaranteed no less than 50% of merger benefits. We disagree. Estimates are estimates. Sometimes a confidence interval can be placed around an estimate. A confidence interval does not invalidate an estimate. Because a confidence interval is stated, we are not required to use the highest point of the interval when applying § 854. Nor are we compelled to use the lowest point of the range. Rather, our task is to use the best evidence and data in this record to determine short- and long-term economic benefits, with no less than 50% of those benefits going to ratepayers. We do that here.

Finally, despite all the evidence comparing mergers, we are not convinced that benchmarks from other mergers are determinative of the amount of savings achievable in this merger. Companies are unique, and offer different levels of efficiencies and opportunities when they merge. The benchmarks provided here demonstrate that applicants' estimate is within a reasonable range, but do not justify the adjustment recommended by TURN.

3.2.3. Additional Best Practice Savings

ORA contends that applicants have failed to include $600 million in best practice savings identified by Mercer. According to ORA, this $600 million is in addition to the $2 billion in expense savings. We disagree.

The Mercer study clearly states that the total expense savings are $2 billion, including best practices. This is reported in the Executive Summary. It is also stated in the "Summary of Synergies: Cost." Nowhere does the study claim a total of $2.6 billion.

ORA correctly points out that on a backup page related to cost synergies Mercer identifies $600 million in potential additional best practice savings for GTE. The backup page first identifies the base estimate of GTE's annual best practice savings that are included in the $2 billion total. The $600 million is then stated, but is qualified. For example, it is noted that the merger "could" provide the additional $600 million savings. The savings are noted as "approximately" $600 million (unlike the base estimate, which is not there stated as approximate). The approximately $600 million is included as a "potential" from a remaining "opportunity."

The base amount is further explained on the next page of Mercer's report, with five specific areas identified. The possible $600 million of additional "potential opportunity" is not explained in any further detail.

We conclude that the $600 million is more in the nature of a range of cost savings. Mercer did not include the $600 million in its statement of total best practice savings. It is the total which we understand to be Mercer's best estimate.

Moreover, Mercer used Automated Reporting Management Information System (ARMIS) data from other telecommunications companies to identify best practice savings (i.e., savings that could result from bringing one company's level of efficiency up to the other company's level, or each company's level of efficiency up to the industry average). As applicants point out, however, this has the potential to lead to erroneous conclusions, since expense data in ARMIS is not always completely compatible across companies on a line-by-line basis. For example, Mercer concluded that Bell Atlantic would be able to achieve over $1 billion dollars in saving, or 65% of its entire cable and wire maintenance expense budget, if Bell Atlantic could bring its level of efficiency (as measured by ARMIS) up to the industry average. GTE's senior management, however, found elements of Mercer's estimates, such as this, not credible, and applied their own judgment to reach their conclusions.

Applicants state that GTE had reviewed and rejected Mercer's methodology to estimate best practices in an earlier engagement.[18] ORA argues that GTE's judgment to exclude $600 million from this second study begs the question of why Mercer was commissioned a second time to corroborate applicants' merger

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[18] Mercer was first commissioned by GTE in 1997. Mercer was hired again in 1998. It is the 1998 study that ORA relies on for the $600 million additional best practice savings.

synergy estimates. ORA concludes that the Commission should be wary of applicants' attempt to repudiate Mercer's findings.

To the contrary, we accept GTE's explanation that GTE engaged Mercer for the second study to analyze the reasonableness of GTE's estimate of revenue synergies. As GTE's Shuell testified, GTE would never have asked Mercer to study cost savings again if GTE had known that Mercer would simply recycle and repackage its earlier study.

Thus, we find a reasonable reading of the Mercer study, including best practice savings, to show Mercer's estimate of total expense savings to be $2 billion, not $2.6 billion. Even if Mercer had included the $600 million of additional best practice savings in its total, applicants' estimate is $2 billion of total expense savings, not $2.6 billion. ORA presents insufficient justification to reject applicants' estimate, and adopt a consultant's estimate, when applicants' estimate is based on the collective judgment of applicants' senior executives with extensive knowledge of each particular company's operations.

3.2.4. Savings Allocation Based On Efficiency

Applicants allocate results in the following ways, which we find reasonable. Applicants allocated joint savings to affiliates and business units by using allocation methods that GTE employs today. Those methods are consistent with the cost allocation methods routinely used by Bell Atlantic. The $2.5 billion estimate of gross cost savings is projected across all operations of GTE and Bell Atlantic. The identified savings categories are: regulated telephone operations, G&A expenses, and capital savings.

For regulated telephone operations, GTE's share was determined based on the percentage relationship of GTE regulated telephone operations for the "big three expenses" (i.e., plant specific, plant non-specific, and customer operations) compared to the same big three expenses for GTE and Bell Atlantic combined.

Based on 1998 expense data, this results in 33% of the savings being allocated to GTE, and 67% being allocated to Bell Atlantic.

For G&A savings, applicants used the percentage relationship of GTE's total operating expenses and taxes to the total operating expenses and taxes of GTE and Bell Atlantic combined. This again relies on the same factors that are used to allocate GTE's G&A expenses to its operating subsidiaries today. Based on 1998 expense data, this results in 45% of G&A savings being allocated to GTE, and 55% being allocated to Bell Atlantic.

Capital synergies were identified for telephone operations, long distance, wireless and internet business units. Capital synergies were allocated using the big three expense allocator since relevant capital synergies relate to telephone operations.

We find applicants' method reasonable because it is based on the extent to which the two companies today consume centrally provided services. As the companies realize savings associated with these common services after the merger, the combined per unit cost of providing a service will be reduced. This reduced expense is best assigned to the entity that benefits from the service in proportion to how much of that service is consumed by each company.

Further, applicants' method uses techniques generally prescribed or approved by the Federal Communications Commission (FCC) and state commissions. The method is consistent with GTE's Cost Allocation Manual, which has been approved by the FCC and is on file with us. After the merger, the overall structure of the combined company will be similar to the one that exists today for GTE: a holding company parent with operating subsidiaries where common services are provided centrally. The existing allocation method will be used to record the actual merger costs and savings on the financial books of GTE California. The savings should be allocated in a consistent manner, reflective of the relative consumption levels for those services by the various entities within the combined holding company. Applicants' method accomplishes this.

TURN asserts that the more inefficient company will disproportionately benefit from the merger. Therefore, TURN recommends allocating joint cost savings between GTE and Bell Atlantic according to each company's relative efficiency. TURN proposes using expenses per access line as a simple proxy for each company's efficiency.

We decline to adopt TURN's proposal. Allocation based on efficiency fails to account for the fact that a greater portion of the savings associated with common cost functions will be achieved by the company that utilizes or consumes more of that function, as discussed above and captured in applicants' methodology.

Moreover, as discussed above, we are not persuaded that GTE is less efficient. GTE's expenses per line, even if higher than Bell Atlantic's, may be higher due to a number of factors. These factors are not always within GTE's control, and do not necessarily reflect greater inefficiency.

For example, an important factor causing differences in costs is the nature of a utility's service territory. GTE's territories are generally more rural than Bell Atlantic's. There may be reasonable cost differences between companies that serve rural versus urban populations.

TURN argues that explaining away relative efficiencies by the difference in serving rural versus urban populations is contradicted by the Mercer study. TURN cites an example from the Mercer study where GTE's costs per line are greater than Bell Atlantic's even after having been controlled for density.[19] On the other hand, the Mercer study also shows that GTE's operating costs per access

[19] TURN cites Exhibit 300, p. 35 (TURN's Opening Brief, p. 16.)

line are lower than those of Bell Atlantic ($34.07 per month versus $35.34 per month, respectively). Further, the Mercer study shows that in two of four cost categories (i.e., cable and wire, and central office transmission), all the savings will flow to Bell Atlantic, not GTE. Nowhere does Mercer conclude that, as a general matter, GTE will achieve a disproportionate amount of the savings.

TURN further argues that Bell Atlantic gets the majority of merger savings under applicants' allocation simply because it is the larger company, despite the fact that GTE is, according to TURN, known to be relatively inefficient. TURN says GTE has the much greater potential to achieve efficiency gains. In support, TURN says Bell Atlantic has already been strengthened due to its merger with NYNEX. Further, TURN says the Bell Atlantic/NYNEX merger has already allowed Bell Atlantic to identify and implement best practices.

We are not persuaded. GTE's merger with Contel provided GTE some of the same opportunities and benefits that Bell Atlantic enjoyed from its merger with NYNEX. Further, in 1992 GTE initiated a five-year Process Re-Engineering Program. As part of that effort, GTE interviewed 85 companies, from which best practices were gathered, analyzed, and implemented. As a result, GTE significantly changed the way it does business. That program was regarded as one of the most successful re-engineering efforts in American business, and resulted in achieved cost savings of approximately $1 billion.

TURN provides an example of an efficiency improvement for GTE which TURN contends shows the fallacy of applicants' methodology.[20] We are not

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[20] TURN's example assumes Bell Atlantic uses an engineering function 700 times per month pre-merger, and GTE uses the same function 300 times per month pre-merger, at a cost to Bell Atlantic of $25 per time (700 times $25, or $17,500 per month) and at a cost to GTE of $50 per time (300 times $50, or $15,000 per month). The pre-merger total cost is $32,500 ($17,500 plus $15,000). Using applicants' methodology, TURN says the savings

Footnote continued on next page

convinced. TURN's example, if correct, would justify applying all of the savings to GTE. Not even TURN's proposal recommends that. The example only demonstrates that there are other approaches to determining how savings may be allocated. For all the reasons stated above, we are not persuaded by TURN's example that TURN's efficiency-based allocation is superior to applicants' methodology.

Even if we were inclined to consider using efficiency as the basis for allocating the savings—which we are not—TURN's proposal incorrectly assumes that all cost savings depend on the relative efficiency of each company. To the contrary, applicants identify three enablers of cost savings: elimination of redundant functions, economies of scale and adoption of best practices. When redundant functions are eliminated, efficiency has little to do with how savings should be allocated to each firm. For example, having one general counsel rather than two will result in savings, but the relative efficiencies of GTE's and Bell Atlantic's respective pre-merger legal departments (or each company's pre-merger overall efficiency) is not a reasonable basis for allocating the savings from this elimination of duplicative function. On the other hand, a reasonable way of apportioning the cost savings is to examine the amount of legal services consumed by GTE versus those consumed by Bell Atlantic, and to apportion the savings in the same manner as how the reduced costs would be apportioned. This is what is done by applicants' methodology.

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would flow 54% to Bell Atlantic ($17,500/$32,500) and 46% to GTE ($15,000/$32,500). TURN says the saving result from GTE implementing Bell Atlantic's more efficient practices, however, and should be attributed entirely to GTE. That is, TURN says the savings comes from reducing GTE's $50 unit cost to $25 per unit. The resulting savings is $7,500, according to TURN, and should be allocated entirely to GTE.

Similarly, savings achieved through economies of scale should not be apportioned according to relative efficiencies of the companies. Rather, such savings are realized through the scale achieved jointly by both companies as a result of the merger. They are not the result of one company simply becoming as efficient as the other in performing a function, or producing a unit of output.

Thus, we find applicants' allocation is the most reasonable.

3.2.5. Transaction and Implementation Cost Allocation

Applicants estimate two types of costs that will be incurred to consummate the merger and integrate the two companies: transaction costs and implementation costs. Transaction costs are necessary so the merger can be consummated. These include costs for performing due diligence in connection with the merger, of preparing regulatory filings, and developing retention agreements with key management personnel to assure continuity of management throughout merger implementation. Applicants estimate total transaction costs of $375 million, with GTE's share being $215.5 million.

Implementation costs are incurred to integrate GTE and Bell Atlantic after consummation of the merger. These include costs of severance and relocation, information systems, establishing the new name ("branding"), real estate consolidation, and departmental integration. Applicants estimate that implementation costs will range from $1,225 million to $1,625 million, and propose using the midpoint of the range ($1,425 million). Of this amount, applicants estimate approximately $1,064 million will be incurred for regulated operations, of which $740 million are associated with telephone operations, and $324 million are associated with G&A functions.

No party proposes an alternate estimate of merger-related costs. These costs were developed by applicants' senior executives, who took into account the nature of the expected savings, along with their knowledge of the two companies' operations. The estimates were made to provide accurate information to shareholders, and were included in the proxy statement required by the Securities and Exchange Commission (SEC). We adopt these estimates.

Applicants directly assign transaction and implementation costs where possible. Remaining costs were allocated between GTE and Bell Atlantic, within GTE to GTE California and other subsidiaries, and then to GTE California's Category I and Category II services, using the same methodology used to allocate cost savings. Except for ORA, no party proposes an alternative allocation of merger-related costs between GTE and Bell Atlantic, or between the various business lines of the companies. ORA, however, recommends that transaction and implementation costs be allocated between GTE and Bell Atlantic in direct proportion to the estimated expense savings. ORA argues that ratepayers should only be required to pay merger costs in proportion to the benefits they receive from the merger. We decline to take ORA's recommendation for the reasons explained below.

3.2.5.1. Transaction Costs

ORA contends that the effect of applicants' allocation is to assign proportionately more costs to ratepayers than their share of benefits. For example, ORA says applicants have allocated $215 million (57%) of the $375 million total transaction cost to GTE, with $168.1 million (or nearly half of the total $375 million transaction costs) to GTE's regulated operations. By comparison, ORA says GTE represents only about one-third of the merged entity based on access lines.

ORA asserts that transaction costs are estimates and, as with any estimate, can and should be allocated in a manner to equitably distribute costs. Transaction costs are incurred to facilitate the whole transaction, not specific parts, according to ORA. ORA says transaction costs have nothing to do with individual services, activities, or business segments. Rather, they are incurred for the best interests of both merger partners, and ratepayers should only pay in proportion to benefits.

We disagree. A significant part of transaction costs are costs that GTE, and GTE alone, will incur. That is, they are not jointly incurred costs that should be allocated to one company or the other. Rather, they are separately estimated costs that are incurred solely by GTE, will be reflected on the books of GTE, and will be charged against GTE's respective, separate earnings. As such, it would be unreasonable to allocate a portion of these costs to Bell Atlantic, as ORA recommends.

Further, the fact that some of these costs have not yet been incurred does not affect which company will incur them, and the company to which they should be attributed. Whether incurred now or in the future, these costs will still be reflected on the books of GTE, and charged against GTE's earnings.

Moreover, it is reasonable to allocate remaining transactions costs in the same way as G&A expenses are allocated. Transaction costs facilitate the entire transaction, just as corporate overhead functions benefit the entire operation of the corporation. The allocation factors used to assign G&A expenses to various lines of business within GTE provide a reasonable basis to allocate transaction costs. Expenses for G&A are allocated within GTE to various entities according to the amount of work done for the benefit of that particular entity, based on a study conducted each year. This method of accounting for expenses of common functions that cannot be directly assigned is consistent with FCC and Commission regulatory practices.

ORA also contends that many transaction costs (e.g., fees to investment bankers, payments to financial advisors, retention compensation paid to senior executives, proxy statement printing costs, shareholder meeting costs) are all made for the best interest of both merger partners. For example, once the merger is consummated, ORA says GTE's costs to persuade its senior executives to remain with the merged entity will confer benefits on the merged entity as a whole, not just on GTE.

To the contrary, financial advisors were separately retained by GTE and rendered an opinion to GTE's Board of Directors. Those costs are properly attributed to GTE. GTE's retention agreements were made many years before the merger with Bell Atlantic was proposed. Thus, even if the merger triggered retention agreements, they reflect decisions made long ago by GTE's shareholders to hold on to senior management during times of change. These costs are reasonably attributed to GTE, and used to offset GTE's portion of merger savings.

3.2.5.2. Implementation Costs

ORA also objects to applicants' allocation of implementation costs. ORA says applicants propose about 75% ($1,064 million) of the estimated $1,425 million be charged to regulated operations, while just 60% of the $2 billion in expense savings is earmarked for regulated services.

ORA asserts that implementation costs can be specifically allocated to individual business segments in theory, but in this case they are more appropriately addressed at the aggregate level. ORA states that the valuation and negotiation of the entire merger is based on aggregate synergies. Viewed only at the ratepayer level, ORA claims valuable mergers might not be approved. For example, ORA says a merger with total synergy benefits exceeding total costs would benefit shareholders, but would be rejected by the Commission under § 854 if allocated ratepayer benefits were less than allocated ratepayer costs. ORA claims the same principle should apply here. That is, according to ORA, implementation costs should be viewed in the aggregate, and implementation costs should be allocated to regulated operations in proportion to the savings being realized.

We decline to adopt ORA's recommendation. Applicants' method of allocation already ensures that implementation costs bear a reasonable relationship to the amount of savings in each category of operations. Applicants have assigned implementation costs to various lines of business based on an estimate of the costs as a percentage of the savings associated with that line of business. That is, for example, total implementation costs assigned to telephone operations are 82% of the annual savings estimated to be realized in that category, just as the costs assigned to wireless and directory categories are 82% of the annual savings estimated in those categories.

Further, ORA's recommendation would shift costs needed to generate savings in regulated operations to unregulated operations. This is equivalent to allocating to ratepayers some of the net savings of unregulated operations. We decline to do this.

Moreover, we reject ORA's conclusion that potential mergers would be rejected even if beneficial overall, but not apparently beneficial to ratepayers. To the contrary, as long as total benefits exceed total costs, a merger is beneficial, and may be considered for approval. In such case, ratepayers may receive benefits through competitive or unregulated services that may justify approval of a merger, even if a specific surcredit on regulated operations is not adopted.

ORA argues that applicants' method improperly and unfairly burdens GTE California's ratepayers, and impermissibly decreases the amount of benefits below the 50% required by § 854. We disagree. Since the adopted allocation does not improperly and unfairly allocate costs to GTE's ratepayers, it does not decrease benefits below the 50% requirement.

3.2.6. Expense or Amortize Costs

Applicants' NPV estimate is based on expensing costs as they occur. As ORA points out, applicants expense costs over three years, and propose four years for the period over which benefits will be generated and distributed to ratepayers. ORA says applicants' approach unreasonably burdens ratepayers with the recovery of all costs within three years, while limiting benefits to only four years.

ORA claims that merger benefits will actually exist over 15 years.[21] ORA asserts that cost recovery should be over 15 years, no matter how long the period for returning benefits to ratepayers. ORA concludes that this will provide consistency in the calculation, and avoid a disproportionate offset of merger savings in the early years. Applicants oppose ORA's methodology.

We decline to adopt ORA's proposal. ORA's recommendation effectively capitalizes transaction and implementation costs, and depreciates these costs over the life of merger benefits. Merger-caused transaction and implementation costs, however, include such items as professional fees, investment banker fees, regulatory fees, and employee related expenses (e.g., retention, relocation, severance). These costs are in the nature of expenses, not capital additions.

Applicants argue that generally accepted accounting principles (GAAP) require applicants' proposed treatment. ORA correctly responds that the Commission is under no legal or regulatory requirement to use GAAP for ratemaking. Rather,

> "...the prime determinate of the course the Commission should take is not what generally accepted accounting principles require but what is fair and reasonable from a

[21] ORA calculates this to be the mid-point of the benefits period used by Salomon Smith Barney, applicants' financial analysts responsible for an estimate of merger benefits adopted by GTE and Bell Atlantic and used in the Joint Proxy Statement.

regulatory viewpoint." (San Diego Gas & Electric Co. and So. Cal. Edison Co. (1978) 84 CPUC 133, 1443, D.89113.)

We sometimes elect to amortize expenses for ratemaking.[22] That, however, is not reasonable here. Rather, the net present value methodology sufficiently takes the timing of costs and benefits into account. No further amortization of costs or benefits is necessary.

The more important factor for the net present value calculation is the determination of the period over which costs and benefits are estimated, pursuant to § 854. ORA proposes using 15 years for its recommended capitalization and amortization. Use of any period less than 15 years for the return of long-term economic benefits to ratepayers under § 854, however, would produce an inconsistency between (a) the period over which costs and benefits would occur and (b) the long-term for § 854. As discussed below, we adopt a period less than 15 years for the long-term under § 854. We similarly decline to adopt ORA's proposal to capitalize and amortize transaction and implementation costs over any period longer than our adopted long-term. To do otherwise would produce an incomplete reconciliation of costs and benefits over whatever term is found to be the reasonable long-term period.

GAAP provides that:

> "all expenses related to effecting a business combination accounted for by the pooling-of-interests method shall be deducted in determining the net income of the resulting combined enterprise for the period in which the expenses are incurred." (Exhibit 6, p. 5, citing paragraph 58 of Accounting Principles Board Opinion No. 16.)

[22] For example, in general rate cases we have amortized non-recurring extraordinary expenses over three or more years when doing so is fair and reasonable.

Applicants state that this merger is intended to qualify as a pooling-of-interests. While we are not required to apply this GAAP standard for ratemaking, it is reasonable to do so here consistent with treatment for the intended pooling-of-interests.

Finally, in the Telesis/SBC proceeding we considered but declined to adopt an amortization of merger-related costs. TURN there argued that large costs in the early years when savings were realized slowly would result in an underestimation of the long run benefits of the merger. (D.97-03-067, 71 CPUC2d 351, 370.) Nonetheless, we treated costs as they occurred, and offset those cost by benefits as they occurred. (D.97-03-067, 71 CPUC2d 351, 417; Table 1, p. 1, footnote 2; p. 2, column "Implement.") We are not persuaded that we erred in the SBC/Telesis merger decision. No reason presented here now compels a different approach.

3.2.7. Revenue Synergies

3.2.7.1. Revenue Synergies as Economic Benefits

Applicants expect revenue synergies (increases) of about $2 billion as a result of the merger. These synergies come from increased sales of vertical services. ORA and TURN argue that revenue synergies are economic benefits of the merger, and must be shared with ratepayers pursuant to § 854. Applicants disagree. ORA and TURN, however, are correct.

Section 854(b)(2) requires that applicants share the "economic benefits" of the merger with ratepayers. Revenue synergies are as much an economic benefit as cost savings. That is, just as cost savings are an economic benefit by increasing net revenues and profits, revenue synergies are an economic benefit by increasing net revenues and profits.

Indeed, the Joint Proxy Statement cites significant revenue synergies as one reason that the GTE Board of Directors recommended shareholders vote in favor of the merger. Annual revenue synergies (increases) were there cited at the same $2 billion level as the annual expense synergies (decreases). Revenue increases were, therefore, an equally important factor as expense savings in the rationale given by management to shareholders for their consideration in approving or rejecting the merger. There can be no reasonable doubt that revenue synergies are an economic benefit.

Applicants argue that we have never ordered increased revenues to be included in benefits and shared with ratepayers, and that we should not do so now. To the contrary, whether revenue synergies have or have not been included in the consideration of previous mergers, the statute is the source of the term "economic benefits," and there is nothing in the statute that limits the definition of the term to exclude revenue synergies. As a practical matter, none of the applicants in prior mergers quantified revenue synergies, or proposed they be shared with ratepayers. Moreover, as TURN asserts, no party has ever recommended inclusion of revenue synergies in a merger proceeding, even if revenue opportunities were discussed generally. Simply because we have not previously required that revenue synergies be quantified and shared does not foreclose their consideration now. In fact, we have never specifically decided the issue against inclusion of revenue synergies. This record, on the other hand, contains a well-developed discussion and quantification of the matter, and it is now ripe for decision.

Applicants assert revenue synergy estimates are inherently speculative, and much less reliable than estimates of cost savings. Cost savings are typically well understood and can be projected with some level of accuracy, according to applicants.

To the contrary, parties have estimated revenues during general rate cases and other proceedings for decades, and we have adopted test year revenues in numerous cases. While there may be some element of speculation with all forecasts, we do not find revenue estimates so unreliable that we must only treat them qualitatively. Moreover, applicants considered the quantification of revenue synergies sufficiently reliable to use them (along with expense synergies) in their Joint Proxy Statement to shareholders, and in their decision to merge.

Applicants also claim that revenue synergies need not be quantified and shared because the revenue increases derive from increased sales, and, according to applicants, consumers already get benefits (i.e., the consumer surplus) from the increased use of a service that they did not previously consume. In response, TURN argues that both consumer and producer surplus are benefits, they both should be quantified, and they both should be shared. TURN concludes that there is nothing about the concept of consumer surplus that means ratepayers are not entitled to an equitable allocation of the net revenues GTE will achieve as a result of the merger.

We conclude that we need not quantify consumer surplus. Consumers enjoy the consumer surplus when they buy an incremental or new service from the merged utility for which they would have paid a higher price. Consumers receive 100% of the consumer surplus.[23] Similar to consumer surplus, unless shared, applicants retain the entire amount of producer surplus.

TURN argues that consumer surplus must be shared because GTE might employ a more perfect scheme of price discrimination with incremental sales, and ratepayers might not get the consumer surplus they deserve. To the contrary, applicants correctly point out that the prices for the vertical services at issue here are tariffed rates, and GTE cannot price discriminate.

[23] Section 854(b)(2) provides that ratepayers shall receive not less than 50% of the benefits of the merger. Ratepayers may receive 100% of the consumer surplus without conflicting with § 854.

ORA argues that, if we decline to include revenue synergies, we should still consider the decrease in unit (average) costs realized by applicants which result from incremental increases in sales and revenues. That is, revenue synergies decrease unit (average) costs, and decreases in costs are an economic benefit, according to ORA. We need not, however, consider including the decrease in unit costs as recommended by ORA since we include revenue synergies directly.[24]

3.2.7.2. Amount of Revenue Synergies

Applicants, ORA and TURN agree that revenue synergies, if included, are the revenues enhancements from vertical services.[25] ORA and TURN, however, believe that all revenue synergies attributable to vertical services should flow to GTE since Bell Atlantic has higher penetration rates for vertical services than GTE. According to ORA and TURN, adoption of Bell Atlantic's best practices

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[24] Even if we were inclined to consider the decrease in unit costs, we would be unlikely to include them in revenues. ORA contends that the decrease in unit cost is "roughly equal" to applicants' revenue increase. (ORA Reply Brief, p. 9.) Roughly equal is not equal. Moreover, we are not convinced that the unit cost decrease would even roughly equal the revenue increase. That is, we agree with applicants that the record simply does not adequately explain why there should be an equivalence between unit cost decreases and revenue increases. In fact, we think that revenue increases might equal cost decreases only if the operating expense margin is 50%. The record shows, however, that the operating expense margin is not always equal to 50% for the vertical services which will lead to revenue synergies. Thus, we are not inclined to consider unit cost decreases resulting from revenue synergies as estimated by ORA for inclusion with economic benefits. We are, however, convinced that revenue synergies themselves are an economic benefit of the merger and should be included directly.

[25] Further, TURN originally proposed, but now agrees to exclude, revenue synergies from the following types of services: large business local, internet dial-up access, internet dedicated access, and internet data transport. ORA originally included, but now excludes, voicemail. ORA originally proposed a small operating expense margin, but now accepts applicants' operating expense margin in year 3.

by GTE will increase GTE's penetration rates to those of Bell Atlantic. ORA and TURN recommend application of Bell Atlantic's nationally based numbers, with an appropriate allocation to California. Applicants, on the other hand, argue that only the net revenue synergies that are attributable to GTE California should be included. We agree with applicants.

Applicants' estimate of total revenue synergies is based on the assumption that the gap in penetration rates between GTE and Bell Atlantic will be closed. That is, the generally lower penetration rates of GTE will be increased to those of Bell Atlantic. On a national level, this may make sense. It does not make sense, however, to simply adopt this same method for assessment of the effect in California.

For example, applicants correctly point out that GTE California's penetration rates for vertical services are actually higher than Bell Atlantic's penetration rates, except for Auto Call Return (Star 69). Only the lower penetration rate for auto call return provides an opportunity within California for revenue enhancement by bringing the rate up to that of Bell Atlantic.

California-specific experience is also relevant for Caller ID. In 1998, approximately 60% of GTE California' residential customers had complete Caller ID blocking. This percentage is nearly twice as high as the next highest state for GTE, and compares to 3% in Texas and 0% in Florida. Accordingly, simply adopting Bell Atlantic's marketing practice with respect to Caller ID is not likely to have the same effect in California.

ORA argues that, while penetration rates fluctuate between states, Bell Atlantic is more successful overall than GTE in marketing vertical services. ORA asserts that it is reasonable to expect an increase in penetration rates in all states, including California, following the adoption of Bell Atlantic's best marketing practices.

ORA makes this claim assuming that the same methods are used by the marketing departments in all states, regardless of whether penetration rates for vertical services in California exceed the national average. We are not convinced. Marketing need not be national only. Rather, it may be state or region specific. Even if applied nationally, we think state specific experience is important in reaching a reasonable estimate. National advertising will not necessarily have the same result in each state or region.

Neither ORA nor TURN provides factual support for their assertion that the adoption of Bell Atlantic's best marketing practices in California will make GTE California even more successful than it has been in the past with respect to penetration of vertical services, no matter how GTE California's penetration rates compare currently to Bell Atlantic's national average. We decline to accept their unsupported assertion.

TURN contends that recent successful efforts to boost Caller ID sales by Pacific Bell (Pacific) is proof that the merged entity will also find ways to make Caller ID more profitable. Therefore, TURN rejects applicants' arguments for the exclusion of Caller ID based on state specific analysis.

We think otherwise. As TURN's reply brief says, the SEC filings show Pacific reporting large increases in sales for vertical services, including Caller ID. TURN does not show, however, how much of that increase is from Caller ID compared to other vertical services. Further, there is no information about how much of that increase has resulted from Pacific adopting SBC's marketing programs, as opposed to developing a new marketing approach, or other effects. Applicants may jointly develop marketing approaches to Caller ID that are different than Bell Atlantic's existing practices in order to take into account unique circumstances in California. Any resulting increase in penetration would not be the result of GTE simply adopting Bell Atlantic's marketing practices. GTE might develop the same program on its own (without the merger), or sales might increase due to other effects.

ORA criticizes applicants' state specific analysis for revenue synergies when applicants rely on a national basis (with allocation to California) for expense and capital synergies. Thus, ORA argues that its national basis for revenue enhancements (with allocation to California) is reasonable.

We think a state specific analysis for all elements of the merger might be an improvement. We decline to reject the state specific analysis for revenue synergies simply because a state specific methodology was not used by any party for expense and capital synergies.

For all these reasons, we agree with applicants. Applicants estimate that increasing the penetration rate for GTE California to that of Bell Atlantic for Auto Call Return (Star 69) will enhance revenues in California by $2.375 million over 4 years. We adopt this result. (See Attachment B.)

3.2.8. Short-Term and Long-Term Periods

Section 854(b)(2) requires an equitable allocation of the short-term and long-term economic benefits. The economic benefits vary greatly depending upon the number of years used for these periods, and in particular the long-term. This may be the single most important variable in the analysis. Parties disagree over the number of years that should be used.

Applicants recommend two to three years for the short-term, and four years for the long-term, to commence with consummation of the merger. Applicants make this proposal based on their perception of the accelerating pace of change in the technological and competitive environments they face, and their belief in the general inability of any entity to predict the state of the industry with any degree of confidence beyond four years. Moreover, applicants say four years will end at the same time as the 5.6 years adopted for the long-term in the SBC/Telesis merger, at which time both service areas will be competitive.

ORA contends that short-term is the period leading up to the onset of effective, price-constraining competition in the local exchange market, while long-term is the period commencing with the onset of effective, price-constraining competition. ORA proposes that the net benefit be returned to ratepayers by a fixed surcredit calculated using costs and benefits over 15 years. According to ORA, the surcredit would apply into perpetuity, but would be applied to fewer services—and eventually eliminated—as services become competitive and are recategorized to Category III. ORA contends that in this way the market, not regulators, will determine the long-term, and removal of the surcredit will be self-implementing. In the event the Commission does not adopt this approach, ORA says costs should be amortized over 15 years, with benefits distributed over eight years. Eight years is a reasonable estimate of when effective, price-constraining competition might arise in California, according to ORA.

TURN recommends that the long-term be 10 years, that benefits be returned to ratepayers by a surcredit, and that services be removed from the surcredit when they are fully competitive (i.e., recategorized to Category III). TURN agrees with ORA that this is a self-implementing way to determine the long-term, and the amount of benefits to share with ratepayers. Alternatively, TURN says that if the Commission adopts applicants' methodology, the long-term period should be no less than 5.6 years, along with adoption of conditions to ensure that competition will be sufficient to bring about the end of rate regulation for all Category I and II services within that period. Specifically, TURN recommends conditioning approval of the merger on GTE's satisfaction of the checklist contained in § 271 of the Telecommunications Act of 1996 (Act - 47 U.S.C. § 271). Alternatively, TURN says the Commission should consider setting benchmarks for measuring whether or not competition has reached sufficient levels in the years following consummation of the merger in order to pass through to ratepayers the guaranteed ratepayer share of benefits.

3.2.8.1. Number of Years

The short-term is the period leading up to the long-term. We have held that the definition of long-term may vary with the circumstances of each individual case. (See, for example, D.91-05-028, 40 CPUC2d 159, 174; D.98-03-073, mimeo., p. 14.) After weighing all the facts and arguments, we find the short-term to be up to five years, and the long-term to be five years, beginning with consummation of the merger.

As we noted in the SBC/Telesis decision, the level of competition is among the principal factors in defining the long-term. (D.97-03-067, 71 CPUC2d 351, 375.) We consider the level of competition not only in a static sense (e.g., current market share, current number of competitors), but also in a dynamic sense (e.g., changes in market share; changes in numbers of competitors; the pace of change in technology, the industry, and the market, including regulatory changes).

We are convinced by applicants here that they face the likelihood of robust competition in California markets, and that technology, the industry, and the market are changing. For example, GTE California began implementing intraLATA toll presubscription in September 1996, and 1-plus presubscription was fully implemented by mid-1997. As a result, GTE California's market share for intraLATA toll has diminished precipitously, and is now less than 50%.

ORA generally agrees, testifying that California will see effective competition in the intraLATA market fairly soon, if it has not happened already. (ORA witness Selwyn, Volume 8, Reporter's Transcript (Tr.), p. 1007:25-27.) Moreover, ORA testified that most residential services provided by GTE California should begin to migrate to Category III within two to three years (ORA witness

Boyd, 10 Tr. 1326:28-1327:13), and that business services will migrate to Category III even more quickly (Id., at 1326:12-1327:18).

We generally agree, and expect competition to develop within the next few years in the local exchange market. For example, we note the dramatic upward trend in collocation arrangements and sales of unbundled network elements (UNEs). While the absolute numbers are still small, they are growing rapidly. Moreover, including pending collocation arrangements, over 62% of GTE California's access lines will soon be available for competition from new entrants.

The extent of competition, however, is not limited to that allowed by interconnections. Rather, competitors are developing important and significant capabilities to bypass GTE California's network altogether. Direct access facilities, cable telephony facilities and wireless facilities owned by competitors are all substitutes for GTE California's wireline service, and will exert increasingly significant competitive pressures.

For example, AT&T's strategy (as evidenced by several acquisitions in the last few years) is focused on cable telephony as a means of delivering a full complement of services to consumers. AT&T's public statements confirm that AT&T expects cable access to be a major avenue of local competition. Particularly noteworthy are AT&T's projections of facilities-bypass relative to use of UNEs as a means of local entry. Sprint's local entry plans involving its Integrated On Demand (ION) network similarly show that GTE's local exchange facilities are only one of many options in bringing this new service to the customer.

In addition, technology convergence will be an increasingly important factor. As AT&T Chairman C. Michael Armstrong explains, convergence will eliminate distinctions among products that previously defined distinct industries, greatly expand the sources of competition, and change the very meaning of telecommunications:

"...we've got to understand the single most significant factor driving our future today. That's why – for all the talk about mergers between companies – the real news is the merger of technologies: The convergence that's driving the Communications Revolution.

"Whether we are talking about the transmission of video, voice or data – we're moving towards a single information opportunity that people will turn to for the variety of services that have always been offered separately.

"As an industry, you may not think of communications as a bunch of smokestacks, but it has been...When you look at where the Communications Revolution is going – it's almost immaterial whether you come at the challenge as a telephone company or a cable company – or for that matter as an Internet company or a computer company. As technology converges, success will go to the company that transforms itself out of the smokestack mentality and into a broad-based consumer services company – a company that can supply consumers with a new generation of communications, information and entertainment services; including some they haven't even heard of yet."[26]

While we believe competition will eventually be robust, we are not as confident as applicants, however, of its vigor within four years. Rather, as TURN points out, competition in GTE's service area may develop somewhat more slowly than in Pacific's service area. For example, GTE is still developing software

[26] Exhibit 25, p. 3 ("Cable Ready: Convergence and the Communications Revolution" C. Michael Armstrong, June 14, 1999). Armstrong's view is shared by Sprint, which says its competitive strategy based on the ION network is "a strategy in which technology simply erases the distinction between local and long distance, and voice, data and video." (Exhibit 15, p. 4 (Sprint's 1998 Summary Annual Report).)

to provide flow-through ordering capabilities for competitors, while Pacific is further along in that process.

Moreover, facilities bypass requires time to become an effective competitive alternative. AT&T's Armstrong is confident that "this future will happen – and it will happen in the next five years." (Exhibit 25, p. 4.) Thus, we think four years may be too short for the long term.[27]

We also think it will take additional time for parties to pursue legitimate assertions through the courts regarding interpretations of the Act, FCC regulations, and other decisions. This may take more than four years, including time to implement court decisions once made.

We also consider the information upon which applicants relied and reported to shareholders. Applicants' financial experts estimated the benefits of the merger over a period of 15 years. GTE argues that this was essentially an extrapolation from the results in year 3, based on assuming nominal perpetual synergy growth rates ranging from 1% to 3% per year. GTE contends reliance on this forecast misconstrues the importance of this simple arithmetic exercise.

To the contrary, if applicants' managements and boards of directors believed the analysis was untrue or unreasonable, they had a responsibility to decline its inclusion in the Joint Proxy Statement to Shareholders. The analysis was

[27] Applicants point out in comments on the PD that Armstrong made his prediction in June 1999, and the five-year period, therefore, ends in June 2004. This justifies adopting a four-year long run here, according to applicants, because the end point of the five-year period reference by Armstrong will be approximately four years away if the merger is consummated in the spring of 2000. We decline to adopt applicants' comment. We are not convinced that Armstrong's prediction is as precise as pinpointing June 2004. Moreover, we direct applicants' attention to Attachment B. Merger benefits to be shared with ratepayers end in 2004. We believe five years remains a reasonable balance of the competing recommendations, particularly when applicants themselves reported benefits to shareholders over a period of 15 years.

included, however, and was based on many more than four years. Management expected shareholders to rely on this information in making their decision. We must take this into account in making our decision.

We also note that applicants agree to fund the CCA over a period of 10 years. That is, applicants have agreed that these benefits may be distributed over 10 years, no matter how long is the period for the generation of benefits from the merger. This is not determinative of the long-term, but is a factor.[28]

We agree with applicants that technological advances and consolidations make the telecommunications industry more, not less, unpredictable than at the time of the GTE/Contel and SBC/Telesis mergers. We differ from applicants on what this means, however. Applicants argue that the increased unpredictability should be reflected in fewer years for the long-term. We think the increased unpredictability argues for more years in the long-term to ensure that we include total economic benefits for ratepayers, as required by § 854.

The state of regulation and ratemaking is another factor in determining the long-term, and is as important a factor as competition. (D.97-03-067, 71 CPUC2d 351, 375.) We concluded in the SBC/Telesis merger decision that this factor supported 5.6 years, and we find here that this factor supports the same timeframe. That is, over approximately the next five years we expect additional changes in regulation and ratemaking. Those changes will reflect more competition and less price-setting by regulators than exists now.

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[28] We note that the Community Partnership Commitment (financed by benefits allocated to ratepayers in D.97-03-067 (71 CPUC2d 351), the SBC/Telesis merger) funds the Community Technology Fund over a period of 10 years. Nonetheless, we concluded the long-term for that merger was less than 10 years.

As we noted in the SBC/Telesis decision, the planning horizon is a secondary factor that may be considered in determining the long-term. (D.97-03-067, 71 CPUC2d 351, 374-375). GTE states that it does five-year strategic plans. (11 Tr. 1481:1.)[29] AT&T's Armstrong mentions five years for the convergence of technologies.

In reaching our decision here, we also consider the long-term found in other mergers. We first note that we have stated several times that the long-term must be determined in each individual case based on the specifics of each case. Nonetheless, even though each was determined separately based on individual circumstances, we have tended to find about five years as the period for the long-term.[30]

Perhaps the most similar recent merger was that of SBC/Telesis. We found the long-term there to be 5.6 years. We think it would be inequitable and unreasonable to find substantially different than 5.6 years for GTE's ratepayers and shareholders than we found for Pacific's ratepayers and shareholders. As such, we decline to adopt a period as long as the eight or 10 years recommended by ORA and TURN, respectively, or as short the four years recommended by applicants.

We also consider the period over which we may make a reasonable forecast, to ensure that we secure the total benefits for ratepayers that are required by § 854 while not exceeding our ability to reasonably predict the future. The pace of change and the inherent uncertainty in regulation, markets and technology led

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[29] GTE reports that it does a five-year plan more as a "habit." (11 Tr. 1481: 24.) Nonetheless, whether or not as a habit, GTE continues to do five-year plans.

[30] We adopted a settlement, and found five years reasonable for the GTE/Contel merger. (D.94-04-083, 54 CPUC2d 258 (1994).) We found 5.6 years reasonable for the SBC/Telesis merger. (D.97-03-067, 71 CPUC2d 351.) We found five years reasonable for the Pacific Enterprises/Enova merger. (D.98-03-073.)

us to reject proposals for 10 and 20 years in the SBC/Telesis proceeding. (D.97-03-067, 71 CPUC2d 351, 375.) These same reasons lead us to reject 8 and 10 years here. At the same time, we are not as unconfident as applicants that we cannot make a reasonable forecast past four years. Applicants' financial advisors made a forecast for 15 years. While we decline to extrapolate that many years, we are confident that we can make a reasonable forecast for five years using elements of the analysis from applicants' financial advisors.

We also increase the long-term from applicants' proposed four years to five years because ratepayers suffer if we are wrong in determining the long-term. That is, once the surcredit or other mechanism to share benefits expires, if price-constraining competition is not in place, ratepayers are not assured of any other mechanism for securing the benefits to which they are entitled under § 854. We must select a period that ensures we have captured the total benefits. If markets change dramatically in the meantime, applicants can always apply to eliminate the surcredit early. We will do so if justified.

Applicants warn that if price-constraining competition occurs before the surcredit is eliminated, applicants will return the benefits twice – once through the surcredit, and a second time through the operation of the competitive market. We are not persuaded. If market forces are determining prices before we eliminate the surcredit, applicants can set a price (or seek approval to set a price) that takes the surcredit into account such that the final price to the customer is competitive. That is, applicants may set the price higher by the amount of the surcredit, so that the final price to customers net of the surcredit equals that of the competition. As such, there would be no double pass-through of the benefit, and this is not a concern in determining the long-term period here.[31]

TURN recommends that we find no less than 5.6 years as the long-term. We decline to do so. As we said in the SBC/Telesis decision, we are skeptical of a definition of long-term that exceeds five years. (D.97-03-067, 71 CPUC2d 351, 375.)

Applicants argue that the long-term here should end coincidentally with the 5.6 years adopted for Pacific Bell. That would be July 2003, which, according to applicants, justifies applicants' recommendation of four years after consummation of applicants' merger. We are not convinced. In addition to all the reasons stated above, we think it would be inequitable to find a period 1.6 years (29%) less for GTE than Pacific.[32] Each merger, and the definition of long-term, must be considered on its own merits. On balance, after considering all the facts and arguments, five years is a reasonable definition for the long-term here.

3.2.8.2. Self-Implementing Definition of Long-Term

ORA and TURN recommend adopting a surcredit that would apply into perpetuity. As services become competitive and are recategorized to Category III, it would be applied to fewer and fewer services, and eventually no services. ORA and TURN contend that in this way the market, not regulators, will determine the long-term, and removal of the surcredit will be self-implementing.

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[31] Even if the surcredit is passed through twice—which is not the case—§ 854 requires that benefits to ratepayers be "not less than 50%." A second distribution of benefits to ratepayers for a subset of services that are subsequently competitive for a limited number of years before expiration of the long-term would not conflict with § 854.

[32] 5.6 minus 4 over 5.6.

This proposal is intriguing. Among other things, it eliminates the need for regulators to define the long-term, it relies on our existing new regulatory framework (NRF) structure to implement the § 854 sharing of benefits, and it generally reduces our regulatory involvement in the market. Moreover, it allows the market to define the long-term, and it relies on the market to determine how much should be shared with ratepayers. We decline, however, to adopt this mechanism.

The arrival of price constraining competition and recategorization may not be coincident. Rather, to support an application, an applicant might first collect data on the state of competition (e.g., evidence on market share, ease of entry, ease of exit, elasticity of demand, elasticity of supply). It then takes time for the application to be prepared, filed, processed, and a decision rendered. Applicants state that the decision in the recent application of Pacific to recategorize inside wire was not issued until about 14 months after the application was filed. Pacific also spent time preparing the application before it was filed, according to applicants.

It takes time for an applicant to develop, and the Commission to process, an application. Responsible regulation is not instantaneous. It is unnecessary and unreasonable, however, to build this delay into the § 854 sharing process.

Also, this "self-implementing" mechanism undesirably increases uncertainty, as shareholders and ratepayers do not know when and if sharing will end. It is more reasonable to provide certainty to shareholders and ratepayers of the net benefits subject to sharing by defining a specific long-term period using our best judgment based on the facts and arguments presented here.

In addition, we have not adopted a "self-implementing" mechanism in prior merger proceedings. We will not do so here absent additional facts on the possible advantages and disadvantages. Without better information, it would be inequitable to applicants to initiate this approach now when we have not done so before.

Moreover, relying on recategorization through NRF is a more complex process than fixing a surcredit mechanism now. We believe there is value in adopting the simpler approach.

Finally, we find below that the merger advances competition. As a result of competition, we are confident that ratepayers will still benefit even if we select a number of years that is too few. That is, to the extent applicants retain money that they would otherwise have given to ratepayers, the competitive environment will require that money to be spent on competition, upgrading equipment and entering new markets. Alternatively, it will become return to reward shareholders for the increased risks they are taking in this new environment, thereby ensuring applicants access to additional capital as they face competition. As a result, the most significant benefits of this merger will be price reductions, service improvements, new products, new services, and advances in quality of service all due to increased competition and access to capital. It will not be an additional few cents per month in bill reduction mandated by § 854 that may result by our adopting a "self-implementing" mechanism in place of a fixed period of 5 years. On balance, we need not complicate the process by initiating a new regulatory mechanism for returning benefits to ratepayers.

3.2.8.3. Conditions on Merger Approval Related to Long-Term

TURN recommends that we consider adopting conditions on merger approval to guarantee the return of benefits to ratepayers required by § 854. TURN believes that the existence of price-constraining competition will ensure that ratepayers get appropriate benefits, but that we cannot be certain when price-constraining competition will occur. Without price-constraining competition, TURN asserts only a surcredit will ensure benefits to ratepayers. If a fixed long-term period is used, TURN recommends adoption of certain conditions to ensure the effectiveness of price-constraining competition coincident with the expiration of the long-term. We decline to adopt TURN's recommended conditions on merger approval.

TURN proposes that we consider conditioning merger approval on GTE's satisfaction of the checklist in Act § 271.[33] We see this as a device to bring GTE under the Act when Congress did not do so directly. We will not do this. Rather, we have sufficient regulatory authority and mechanisms to facilitate competition without specifically adopting the checklist in Act § 271 checklist.

Alternatively, TURN recommends that we consider establishing benchmarks for measuring whether or not competition has reached sufficient levels in the years following consummation of the merger to ensure that ratepayers have received their guaranteed share of merger benefits. TURN does not make specific recommendations on those measures, and we will not craft them ourselves.

Moreover, we are not convinced that such measures are necessary as a condition of the merger. Rather, as we have in other merger proceedings, we can determine a reasonable period for the long-term and ensure that ratepayers get the benefits to which they are entitled under § 854 without increasing the regulatory burden on applicants, shareholders, ratepayers, interested parties and ourselves. Should modifications to regulation or the market be required to facilitate competition, we will undertake the necessary initiatives in appropriate other proceedings, or seek adoption of necessary legislation.

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[33] Section 271 of the Act establishes a 14-point checklist that RBOCs must meet before they may engage in long distance service within their local service areas. (47 U.S.C. 271.)

3.2.9. Conclusion

Based on our decisions above, the overall benefits of the merger are $168.1 million (NPV). (See Attachment B.) This is calculated by adding the revenue synergy benefits to applicants' estimates of merger savings over 4 years. We then calculate year 5 by escalating year 4 results using 2%. The 2% factor is the mid-point of the 1% to 3% nominal perpetual synergy growth rates used by applicants' financial analysts and reported in the Joint Proxy Statement. (Exhibit 157, LLS-1, page I-44.)

As a result, we find the NPV of total merger benefits are $168.1 million (NPV). This is $56.4 million (50.5%) more than applicants' recommendation of $111.7 million (NPV).

3.3. Allocation of Economic Benefits to Ratepayers

3.3.1. Percentage

As we have done in other merger proceedings, and as recommended by the parties here, we allocate 50% to ratepayers. In this case, that is $84.1 million (NPV).

3.3.2. Net Present Value Methodology

No party disputes applicants' proposed 10.5% discount rate. The rate is applied on an end-of-period basis, just as we did in SBC/Telesis, bringing costs and benefits back to the beginning of the year. No party proposes otherwise.

3.3.3. Community Collaborative Agreement

Twelve community coalitions representing more than 450 community-based organizations negotiated a Community Collaborative Agreement with applicants. (Attachment C is a copy of the CCA.) Proponents of the CCA argue that it provides unique and important benefits to ratepayers, and all of California, which cannot be obtained in any other way. Applicants, along with Public Advocates, Greenlining and LIF, urge that it be adopted, and that $19.8 million

(NPV) of the ratepayer share of merger economic benefits be used to fund portions of the CCA.

The CCA is premised on the notion that:

> "Vast and important changes are taking place in the telecommunications landscape, with important opportunities to serve the needs of all Californians. This Community Collaborative Agreement specifically seeks to ensure that California's traditionally underserved communities, including low-income, ethnic, minority, limited-English-speaking, and disabled communities in California's various rural, urban, and inner-city regions, will benefit fully and equally along with all of California, from these extraordinary changes." (See Attachment C herein, Preamble, page 2.)

To accomplish this goal, the CCA establishes, extends or modifies programs; states commitments; and identifies objectives. In summary, the CCA provides the following:

1. Community Collaborative Fund: Applicants will provide $2.5 million per year for 10 years, totaling $25 million (nominal dollars), funded from the ratepayer allocation of merger benefits. The funds will be used for under-served community access to telecommunications and information services, education, literacy, telemedicine, economic development and telecommunications advocacy. A Community Collaborative Committee (CCC) will implement and monitor the agreement, but will not be involved in distribution of funds. A third party, nonprofit agency, will administer the fund.

2. Universal Service: Applicants will provide $1.3 million per year for three years, totaling $3.9 million (nominal dollars), funded from the ratepayer allocation of merger benefits. The funds

will be used to continue the Universal Lifeline Telephone Service (ULTS) Partnership[34] for at least 3 years beyond the year 2000. Applicants commit to work towards achieving a 98% universal service goal, including 98% penetration in California's under-served and under-represented communities.

3. Contributions: Applicants will increase their existing California philanthropic contributions by $1 million per year, for a minimum of 4 years, totaling $4.0 million (nominal dollars), funded by applicants' shareholders. One hundred percent of the additional $1 million will be directed to grants for nonprofit community-based organizations serving California's under-served communities.

4. Technical Assistance: Applicants will encourage and support their California employees to donate their time and knowledge to nonprofit agencies that focus on literacy, education, and technology application programs. The support will be in the form of monetary grants to organizations serving California under-served communities to which employees volunteer their time. Applicants will increase their annual budget for this from $60,000 to $150,000, funded by shareholders, for 4 years, totaling $360,000 (nominal dollars).

5. Leadership Meetings: Applicants pledge to hold leadership meetings at least semi-annually with the CCC, community-based organizations, and public interest groups. At least once per year the meeting will include the president of GTE California.

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[34] Applicants created a ULTS Partnership to implement the ULTS directives in D.94-09-065 (56 CPUC2d 117, 258-261).

6. Quality of Service: Applicants pledge to maintain or improve the quality of telephone service in California, including in under-served communities.

7. Diversity

   a. Employment: Applicants commit to continuing to make diversity a critical component in the recruitment, hiring, career development and promotion of all people, including minority, women and disabled employees at all levels, including in the following areas:

      i. Hiring and Promoting: Applicants will hire the best people, including those with diverse styles, backgrounds and skill sets.

      ii. Education and Training: Applicants will support diversity awareness education and skills training for employees.

      iii. Communication: Executive leadership will engage in frequent communications about opportunities and issues related to diversity and its importance to applicants' business.

      iv. Workforce Development: Applicants will provide employees with the technological tools needed to contribute to the success of applicants and their own careers.

   b. Supplier Contracts: Applicants intend to position themselves as an industry leader in contracts to qualified and competitive minority vendors.

3.3.4. Ratepayer Funding of Community Collaborative Agreement

Applicants, along with Public Advocates, Greenlining and LIF, propose that $19.8 million (NPV) of the ratepayer share of merger economic benefits be used to fund portions of the CCA (i.e., the Community Collaborative

Fund, and universal service). No party opposes the objectives of the CCA. In fact, ORA and TURN both say that the goals of the CCA are laudable.

ORA and TURN, however, argue that none of the CCA should be funded by benefits otherwise allocable to ratepayers. Rather, they recommend that the CCA be adopted as a condition of the merger, and thereby funded by applicants.

We adopt applicants' proposal that $19.8 million (NPV) of the cost of the CCA be funded from the merger benefits allocated to ratepayers. We approved this treatment for a similar agreement (the Community Partnership Commitment – CPC) in the SBC/Telesis merger. There are no compelling reasons to adopt a different application of ratepayer benefits here.

The CCA improves on the CPC in several ways that also support its adoption and funding by ratepayers. For example, the CCA provides for the appointment of a third party administrator selected through a request for proposal process, and places a timeframe on selection of the administrator. Applicants pledge that they will file an annual report with the Commission. (Exhibit 1, Chapter VII, pages 16-17; 12 Tr. 1613:12-23.)

Similar to the CPC, the CCA will promote access to telecommunications services in traditionally under-served communities, promote economic development, promote universal service by working towards achieving a 98% penetration rate, promote education, and promote diversity in employment and contracting. It will further our goal of ensuring that California's under-served communities have reasonable access to evolving telecommunications services.

Further, it will accumulate a small surcredit per customer into a fund that provides an overall greater good. For example, achieving the goal of promoting education will benefit not only the person receiving the training, but the state's economy generally by contributing to an educated workforce. Achieving the goal of economic development will benefit not only an individual proprietor, but, through the multiplier effect, benefits others as well. To the extent the goal of increasing penetration to 98% is reached, this increases the benefit of the network for everyone since the value of the network increases to all subscribers when a greater portion of the state's population is connected to the public switched network. (See, for example, D.94-09-065, 56 CPUC2d 117, 139.)

Further, the CCA leverages ratepayer funds of $28.9 million (nominal dollars; $19.8 million NPV). It does this by applicants agreeing to contribute an additional $4.36 million (nominal dollars), or 15% more, from shareholders.

The cost of the CCA to ratepayers is 7 cents per residential customer per month, and 19 cents per business customer per month.[35] While these are small amounts, we do not accept the position of Greenlining and others that even small amounts of surcredits are irrelevant to customers.[36] We have heard from too many thousands of customers over too many years to think otherwise. All customers, particularly those on fixed incomes or with limited resources, care passionately about reasonable rates.

Rates are constantly adjusted in small amounts. If small increases are consistently added to bills, but small refunds are not subtracted, rates will increase unreasonably. (See, for example, D.94-08-030, 55 CPUC2d 689, 697.) No customers, including less affluent customers, are indifferent to paying unreasonable rates.

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[35] Exhibit 33 shows that the difference between the surcredit with and without the community collaborative is $0.07 per month for a residential customer ($0.20 minus $0.13), and $0.19 per month for a business customer ($0.53 minus $0.34).

[36] For example, even 7 cents per month for a residential customer is $4.20 over five years, and 19 cents per month for a business customer is $11.40 over five years.

Greenlining and LIF argue in comments on the PD that the only record evidence here supports a finding that customers prefer fund creation to small surcredits. Greenlining contends, for example, that no other party presented any evidence on customer preferences, while its survey shows that the majority of Spanish surnamed customers, and customers in general, support creation of a fund instead of surcredits. We are not persuaded.

The fact that Greenlining conducted a survey that was introduced into this record does not make that survey determinative of customer preferences. We compliment Greenlining for undertaking the survey, but we decline to rely on its results at this time.

For example, we are concerned that the survey unreasonably led responses. Question 3 was introduced by stating: "Many consumer groups are suggesting that a <u>better</u> use for this monthly rebate would be to establish a Consumer Protection Fund...to <u>protect</u> consumers and customers from telephone <u>fraud</u> and <u>abuse</u> like cramming and slamming." (Exhibit 361, emphasis added.) We believe that this statement likely influenced answers.

Further, we are concerned that Question 3 was inadequately representative of the CCA. That is, while the education and telecommunications advocacy elements of the CCA may address fraud, abuse, slamming and cramming, there is nothing in the CCA that directly and specifically addresses fraud, abuse, slamming and cramming. In fact, we think it likely that the education and advocacy elements will address many things beyond fraud, abuse, slamming and cramming. On the other hand, the CCA directly focuses on such initiatives as under-served community access to telecommunications, literacy, telemedicine, and economic development. The survey, however, does not register reactions to these other activities.

In addition, it is arguably the role of the Commission and law enforcement entities and agencies to prevent and punish fraud, abuse, slamming and cramming.

It is unclear why this should be the major focus of the CCA, or the survey. The CCA will do much more than address fraud, abuse, slamming and cramming.

We are also concerned with other aspects of the survey. The survey was conducted such that a survey respondent could have been anyone in the household answering the telephone, not necessarily the subscriber or someone in the household who would make the economic decisions for the household. This reduces the usefulness of the results.

On the other hand, we have heard from thousands of ratepayers over many years about the importance of every penny in rates and rate reductions. Thus, while we thank Greenlining for their important effort to collect useful evidence, we are not persuaded that we may use that information at this time to find customers generally prefer fund creation to surcredits.

Nonetheless, for the other reasons explained above, the benefits of the CCA justify its adoption and funding by ratepayers. We are authorized under § 854(b)(2) to equitably allocate the benefits between shareholders and ratepayers, such that ratepayers receive no less than 50% of the benefits. Section 854(b)(2) does not require that ratepayer benefits be distributed only by surcredits. An equitable allocation here includes funding of the CCA to the extent recommended by applicants.

TURN argues that the CCA embodies activities and commitments that directly benefit applicants, and that applicants, not ratepayers, should fund the CCA. TURN says, for example, that the $1.3 million annual cost for the ULTS Partnership program is now borne by applicants, whereas the CCA shifts that cost to ratepayers.

TURN is incorrect. We ordered GTE California to implement a universal service plan similar to that previously ordered for Pacific. (D.94-09-065, 56 CPUC2d 117, 260.) GTE California responded by creating the ULTS Partnership.

The Commission's universal service plan included monitoring, marketing plans, budgets, workplans, studies, and more. We indicated that this was required in order to provide information to the Commission on how well universal service goals established by the Legislature[37] are being pursued and achieved, as well as to allow us to prepare our annual compliance report to the Legislature pursuant to § 873(a)(4). Applicants proposed Z-factor treatment for these costs. We rejected the proposal, noting that:

> "...there is no basis for any such request. The need for Pacific and GTEC to provide the Commission with adequate information to monitor their activities, for universal service as well as in other areas, is subsumed within the existing revenue levels." (D.94-09-065, 56 CPUC2d 117, 260-61.)[38]

Further, TURN argues that, if the CCA goals are met (e.g., 98% penetration, economic development), applicants will have more subscribers, earn more revenue, achieve increased goodwill, have better brand identification, and enjoy greater customer loyalty.

While this may be true, this is not a reason to reject ratepayer funding. To the extent quantifiable (e.g., more revenue by increasing penetration from 95% to 98%), these might be benefits that could be shared (just as above we included

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[37] Sections 871-882.

[38] TURN asserts in comments on the PD that GTE California must today recover ULTS Partnership costs from rates. TURN continues, however, that the CCA will produce no change in rates while GTE California will be relieved of the need to fund the ULTS Partnership from rates since it will be funded by the CCA. TURN contends this provides a benefit of $1.3 million to applicants per year for three years. To the contrary, today's decision provides that ratepayers are allocated all appropriate merger benefits. All ratepayer merger benefits, however, do not need to be allocated to ratepayers by a rate reduction. Allocating some of the benefits to ratepayers by a mechanism other than a rate reduction does not mean that applicants are given a benefit of $1.3 million.

revenue from additional vertical sales). No party, however, including TURN, quantified these benefits. We have no record upon which to make our own estimate and increase benefits. We do not know, for example, the existing level of penetration. We do not have an estimate of the extent to which the ULTS Partnership will be successful, and, if successful, the year in which 98% penetration (or more) will be reached.

Moreover, as Greenlining and LIF point out:

> "The harsh reality is that enlightened self-interest is never enough. Intervenor's long-standing experience is that corporations must initially receive incentives to target the underserved, who, in the long run, will prove profitable." (Greenlining/LIF Reply Brief, page 16.)
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> "By definition, if the marketplace sua sponte addressed the needs of underserved communities out of self-interest, there would be no underserved groups in California today." (Id., page 18.)

Thus, even if we had data on increasing penetration rates, we would also need data on profitability and the incentives that are necessary to serve this otherwise under-served market. We have no such data.

Furthermore, TURN focuses on the benefits of the CCA to applicants. There are also benefits of the CCA—just as we found for the CPC—that are enjoyed by ratepayers and all Californians. All benefits (to applicants, ratepayers, and the state) need not be quantified to make a reasonable determination of merger economic benefits, and an equitable allocation of those benefits.

TURN asserts that a core principle of determining merger-related costs and savings is that only incremental effects of the merger are to be considered. TURN contends that applicants will undertake all, or nearly all, of the activities encompassed in the CCA without the CCA, and without the merger. For example, TURN says GTE California is committed to maintaining or improving quality of service, even without the CCA or the merger. Similarly, GTE California already supports community-based organizations (CBOs). As such, TURN concludes that ratepayers should not fund the CCA.

TURN is correct that GTE California is already committed to quality of service and supporting CBOs. The record does not let us precisely determine the level of various activities and commitments before and after the CCA or merger. We believe the CCA, as an element of the merger, furthers applicants' efforts in these areas, and, as such, goes beyond levels that would exist without the CCA or the merger.

TURN argues the CCA includes activities and commitments that are more in the nature of mitigation measures rather than economic benefits to ratepayers. As such, TURN asserts the CCA should be adopted as a condition of the merger, without ratepayer funding.

We disagree. We do not find that the proposed merger creates conditions that must be mitigated in ways provided by the CCA. Rather, to the extent merger conditions or clarifications are adopted, they are adopted for specific matters discussed below.

3.3.5. Clarifications on Adoption of Ratepayer Funding

3.3.5.1. Benefits to GTE California Service Area and Ratepayers

TURN argues that ratepayer funding of the CCA should be rejected because the benefits of the CCA are not limited to the ratepayers of GTE California. We agree with TURN that benefits to be shared under § 854 should generally go to the ratepayers of the merging company (in this case GTE California). We did not apply this limitation in our approval of the CPC in the SBC/Telesis order, however, and do not generally do so here. (See, for example, D.97-11-035.)

Nonetheless, there are relevant differences between Pacific and GTE California that justify slightly different treatment. Pacific serves the majority of the state's telephone customers, while GTE California serves 20% or less of the state's access lines.[39] A benefit provided by the CPC to California under Pacific's program is more likely to be coincident with Pacific's ratepayers. The same is not necessarily true of the CCA for GTE California's ratepayers, unless those benefits are more narrowly focused.

Because of this, we clarify our approval of ratepayer funding of the CCA. Our approval is contingent upon those benefits being focused on GTE California's existing and future under-served population to the extent possible. That is, the $25 million (nominal dollars) in the Community Collaborative Fund, and the $3.9 million (nominal dollars) for universal service, should be spent to address under-served needs in GTE California's existing service area, and among existing and potential future ratepayers, to the extent possible.

We do this by directing the CCC to take this into account in its implementation and monitoring of the CCA. The CCC will give guidance to the contracting agency administering the Community Collaborative Fund, for example. That guidance should include the administrator taking the GTE California service area and its ratepayers into account in awarding money. For instance, funds from the Community Collaborative Fund awarded for under-served community access to telecommunications services, education, literacy, and economic development should generally be for activities within the GTE California service area. This does not mean that CCA money cannot be used to fund activities that will meet the CCA's goals even if some or all of the beneficiaries are outside the GTE California

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[39] Exhibit 37, page 35. GTE California serves 4.6 million access lines (20.4%) out of a total of 22.5 million access lines for GTE California and Pacific Bell combined. There are also other telephone companies in California (e.g., Roseville Telephone Company, Citizens Telecommunications Company).

service area. Rather, this means that if there are two otherwise equally qualified proposals, the administrator should award the money to the proposal that most closely focuses the benefits on GTE California's ratepayers and service area.[40]

This clarification also applies to the contributions ($4 million nominal dollars) and technical assistance ($360,000 nominal dollars) portions of the CCA that are funded by applicants. We apply this clarification to those funds as well because our adoption of ratepayer funding of the CCA is in part based upon, and justified by, applicants' leveraging the ratepayer funds with their own funds.

3.3.5.2. Workplan and Benchmarks

ORA points out that the CCA does not include a means to measure whether its stated commitments are met. TURN says that the performance under the CCA should be compared against a benchmark. We agree with these concerns. For example, we should not expect to see annual reports that compare performance only against a "good faith commitment" (e.g., universal service), "encouraging" employees to donate their time (e.g., technical assistance), "intentions" to maintain and improve the representation of minority employees (e.g., diversity), or "intentions to make a good faith effort to hire minority vendors" (e.g., supplier contracts).

Good faith and intentions are not enough to justify our allocating $19.8 million (NPV) of merger benefits that would otherwise be given directly to

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[40] We specifically do not restrict the allocation of funds to GTE California's service area and customers. As Public Advocates points out, ratepayers may be actual and potential, just as competitors may be actual and potential. Applicants state that they plan to enter and compete in Pacific's service area. Therefore, applicants' potential ratepayers may include ratepayers outside their existing service area. At the same time, the majority of the benefits should be focused on actual and potential under-served ratepayers now in GTE California's service area, to the extent possible, not possible future under-served ratepayers outside GTE California's existing service area.

ratepayers. While 7 cents per month (residential) and 19 cents per month (business), for a total of $19.8 million (NPV), may not be a large amount in some contexts, it should not be squandered.

Public Advocates agrees that the CCA does not set forth precisely how to benchmark and measure progress towards each commitment. Public Advocates claims, however, that the CCA:

> "requires that the Community Collaborative Committee shall monitor and measure GTE's and Bell Atlantic's progress toward each commitment in the agreement throughout the ten years of the agreement." (Opening Brief, page 11; emphasis added.)

We expect measurement to be specific. If the CCC will monitor and measure progress, the CCC can establish specific standards and benchmarks for measurement now.

Greenlining and LIF point out that

> "the Collaborative commitments, however, will not be easily achieved, and will require resources, an ongoing partnership and workplan to reach goals, and oversight by all parties, including the Commission." (Reply Brief, page 19; emphasis added.)

We agree a workplan is necessary to reach goals. Moreover, effective oversight should include measuring success against goals and benchmarks.

Therefore, we require applicants to develop a specific workplan, including standards and benchmarks, for the entire CCA within 120 days of consummation the merger. To facilitate the measurement of the $1 million increase in the contributions portion of the CCA, applicants should include a statement in the workplan showing their actual California philanthropic contributions for the last five years.

Applicants should seek adoption of the workplan by majority vote of the CCC. Whether or not adopted by majority vote, however, applicants should file the workplan in, and serve a copy on the service list for, this proceeding as a compliance filing, with a copy served on the Director of the Telecommunications Division. Parties may file and serve responses within 20 days, with a copy served on the Director of the Telecommunications Division. Applicants may file and serve a reply within 5 days. The Director of the Telecommunications Division may determine whether or not efforts should be employed by the Commission to resolve differences. Annual reports on the CCA should then contain, among other things, a report on the success of the CCA compared to the workplan filed by applicants, including standards and benchmarks.

3.3.5.3. Accountability

TURN proposes modifications to the CCA to increase accountability. For example, TURN recommends that applicants not be on the Selection Committee or the CCC, and that a representative of the Commission be on each committee. TURN says it believes this is consistent with changes to the CPC made in D.97-11-035.

D.97-11-035 removes any utility from participation in the selection of members to a disbursement committee, or to be represented on the disbursement committee, for purposes of the CPC. It also directs that the Commission's Telecommunications Division have oversight responsibility over the disbursements committee.

In comparison, the CCA provides that applicants will have one member on the Selection Committee to choose a non-profit agency which will administer the fund. The Selection Committee is also composed of one representative of Public Advocates and non-intervenor signatories, plus one representative from Greenlining/LIF, for a total of 3 members.

Applicants have only 1 of 3 positions. This provides enough check and balance that we need not eliminate applicants from the Selection Committee. At the same time, there is value in having Commission oversight when money that would otherwise be allocated to ratepayers is involved, just as we did in approving the CPC in the SBC/Telesis merger.

Therefore, we decline to adopt TURN's recommendation to exclude applicants from the Selection Committee. For the purpose of oversight, Commission staff will be notified of, and entitled to attend, each meeting (including executive sessions) of the Selection Committee, review al communications between members of the Selection Committee, review all communications between the Selection Committee (or any member of the Selection Committee) and any applicant for the position as administrator, and review all communications between the Selection Committee (or any member of the Selection Committee) and or any other person or entity. Among other things, that oversight will be used by Telecommunications Division in its review of applicants' annual report, and in making any recommendation to the Commission on the CCA.

We adopt the same approach with the CCC. We decline to delete applicants' representative. For the purpose of oversight, Commission staff will be notified of, and entitled to attend, each meeting of the CCC (including executive sessions), review all communications between members of the CCC, and review all communications between the CCC (or any member of the CCC) and any other person or entity.[41]

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[41] Public Utilities Code Section 583, and General Order 66-C, limit the information that the Commission and its staff may make public when that information is of a confidential nature. This might include some, but not necessarily all, communication between Selection Committee members, CCC members, applicants for the position of administrator, or other persons or entities.

Greenlining and LIF assert that the CCC will have no role in grantee selection. (Opening Brief, page 10.) Public Advocates disagrees that this limitation exists, contending that the CCA does not restrict the role of CCC members. (Reply Brief, page 19, footnote 32.)[42] This is an area in which CCA signatories may or may not have an agreement. Applicants, however, have the same understanding as Greenlining and LIF.

We adopt the view of Greenlining, LIF and applicants as a clarification of our agreement to allocate $19.8 million (NPV) to the CCA. That is, we expect the CCC to establish standards for use by the fund administrator in awarding grants to applicants of Community Collaborative Fund resources. We expect the fund administrator, not the CCC, to make the actual grantee selections. We agree with TURN that this will reduce, if not eliminate, any appearance of impropriety.

TURN also proposes that those serving on the CCC be ineligible to apply for funds, and that we make this condition explicit. Public Advocates opposes this, arguing that Resolution T-16172 addressed and resolved this concern. We agree with Public Advocates.

We do not want to force organizations working on the provision of equal access to under-served communities in California to choose between (a) contributing their expertise and service to California's communities via the CCC and (b) forgoing such contributions to preserve the mere eligibility to propose a project and have it considered on its merits. As Public Advocates says, community leaders likely will not volunteer to provide their expertise, reputation and

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[42] In comments on the PD, Public Advocates say they agree that the non-profit fund administrator, not the CCC, will do the actual selection of grantees.

leadership where such service automatically disqualifies their organization from possible funding for candidate projects.

We expect the fund administrator to make the actual decisions on grantee awards, not the CCC. Therefore, we think there is sufficient separation between members of the CCC and decisions on awarding funds to decline adoption of TURN's proposal.

Relatedly, just as we specified for Pacific and the CPC, one of the criteria we expect the CCC to state for the administrator's guidance in awarding funds is that the funds are to be used to the fullest extent possible to actually meet the objectives (e.g., serving under-served communities), not merely subsidizing the internal operations of the recipient organizations. (D.97-11-035, 1997 Cal. PUC LEXIS 1023, at 9, ordering paragraph 1(b).) Similarly, the recipient's spending will be without restrictions imposed by any signatory to the CCA whose interests may be different from those of the recipient, except to the extent those restrictions are contained in the overall guidelines adopted by the CCC for use by the administrator in awarding funds.

Finally, we expect the CCC to ensure that the administrative costs for the entire administration of the CCA are kept to a minimum. We do not want to see annual reports that reveal an unreasonable portion of the $19.8 million (NPV) of ratepayer funds, or $4.36 million (nominal dollars) of applicants' funds, spent on administration.

3.3.5.4. Unspent Funds

There is nothing about the CCA that limits the amounts to be spent. That is, applicants may decide to spend more, but will not spend less. We also see no reason why the funds will not be spent productively within the stated time periods. Just as we did with the CPC for Pacific, however, we will require unspent funds, if any, that are funded from the benefits allocated to ratepayers to be returned to ratepayers.

Unspent amounts for the purpose of notifying the Commission should also include those amounts funded by shareholders, since we agree to the allocation of $19.8 million (NPV) of the ratepayer share of benefits in part because it is leveraged with shareholder contributions. Should any funds remain undistributed within the time period for those funds (e.g., three years for universal service, four years for contributions, four years for technical assistance, 10 years for the Community Collaborative Fund), applicants should, within 60 days after expiration of the period, submit an advice letter to the Commission, with service on the service list for this proceeding, and a copy served on the Director of the Telecommunications Division. The advice letter should identify the amount of unspent funds, and state a recommendation for their distribution. Parties should have 20 days to serve comments or protests, and applicants five days to serve a response. The Director of the Telecommunications Division will review the advice letter, comments, protests, and response, if any, and prepare a resolution for our consideration. The resolution will adopt applicants' recommendation, adopt another distribution of the funds, set the matter for formal consideration, or otherwise reasonably address the matter.

We do not want to see any significant delay in meeting the goals of the CCA. Therefore, applicants should serve an advice letter on the Commission, with service on the service list for this proceeding and the Director of the Telecommunications Division, within 60 days of the following relevant periods: if the Selection Committee has not selected a fund administrator and initial funds actually disbursed within 12 months of initiation of the CCA; if initial funds have not been distributed for universal service within 12 months of January 1, 2000; if approximately an additional $1 million has not been spent on contributions within

12 months of initiation of the CCA; and if approximately an additional $90,000 has not been spent on technical assistance within 12 months of initiation of the CCA.[43] The advice letter should identify the problems causing a delay, and state a recommendation. Parties should have 20 days to serve comments or protests, and applicants 5 days to serve a response. The Director of the Telecommunications Division will review the advice letter, comments, protests, and response, if any, and prepare a resolution for our consideration. The resolution will adopt applicants' recommendation, adopt a reasonable alternative, or set the matter for formal consideration.

Also, just as we did for Pacific Bell's CPC, we direct that if applicants withdraw for any reason from their CCA financial commitment (including shareholder funds for contributions and technical assistance), the balance of the $19.8 million will be distributed through a billing surcredit over the remainder of the life of the existing surcredit. Applicants should serve an advice letter within 60 days of any such withdrawal, with the same process as explained above for comments or protests and our consideration.

3.3.6. Alternatives for Future Consideration

We adopt the CCA here just as we adopted the CPC for Pacific. We caution, however, that this is not to be considered a precedent for the future. At some point, and some dollar level, it makes sense to let ratepayers themselves decide how they would like to spend their share of allocated benefits, even if it is only a few dollars over the life of the benefit distribution. This is so despite the

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[43] Public Advocates comment on the PD that initiation of the CCA would occur upon Commission approval of the CCA by this decision. We clarify that we here mean initiation for purposes of reporting within 60 days of certain events to be the date of merger consummation.

greater good that can sometimes be gained by pooling money that would otherwise be returned to ratepayers, and despite the leveraged effect of shareholder money being pledged in addition to ratepayer money.

For example, we are intrigued by ORA's suggestion that we might direct applicants to include bill inserts listing organizations to which ratepayers might decide to donate their surcredit. (Reply Brief, page 37, footnote 8.) ORA points out that this might be a system similar to the contribution check-off list that is included on California's income tax forms. This is an innovative proposal, and potentially reduces the "heavy hand" of regulators making decisions for actual and potential ratepayers which might better be made by ratepayers themselves.

We decline to adopt this approach here, however, because it is not sufficiently well developed. We invite additional testimony on this proposal for our further consideration in a future proceeding wherein allocated benefits to ratepayers might be pooled rather than returned.

Similarly, we are intrigued by TURN's proposal that some or all of the $19.8 million (NPV) might be used to reach the under-served by increasing the lifeline discount to low-income ratepayers within GTE California's service area. Alternatively, TURN proposes that it might be distributed more heavily to the residential basic access charge, with lesser portions going to other Category 1 and 2 services. These proposals might meet the needs of the under-served community more directly and better than allocating funds to organizations where an administrative fee must be paid to the fund administrator, and to each organization to which funds are awarded.

Again, we decline to adopt these recommendations here because we have insufficient information. For example, this record does not state how many actual or potential subscribers there are on the lifeline program, how much existing lifeline rates might be reduced by the $19.8 million (NPV), how the funds might be allocated between residential basic access and other services, what might be the effect on rates of an allocation between basic access and other rates, and how rates would be adjusted when the $19.8 million (NPV) is exhausted. We invite additional testimony on such proposals for our further consideration in a future proceeding wherein allocated benefits to ratepayers might be pooled rather than returned.

3.3.7. Surcredit

The benefit to be allocated to ratepayers is $84.1 million (NPV). Of this amount, we allocate $19.8 million to the CCA. The difference is $64.3 million (NPV). We distribute this by a surcredit, just as we did in the SBC/Telesis merger, and as recommended by parties here. The surcredit will be applied over 5 years.

3.3.7.1. Billing Base

Parties differ on the base over which the amount should be allocated. Applicants and ORA propose using the same billing base as the CHCF-B fund. This excludes the basic residential monthly service charge from the surcredit base. TURN recommends including the basic residential monthly service charge. We adopt TURN's proposal.

Applicants' proposal results in residential access line customers who do not use other services widely benefiting less on a total bill basis than customers with charges for high usage, toll or vertical services. They will also benefit less than will business customers. TURN shows that, as of February 1999, a significant number of customers rarely, if ever, make intraLATA toll calls, and only a small percentage use custom calling features. As such, on balance, it is better to ensure that all customers receive a fair share of the benefits by including residential basic access rates in the billing base.

Further, TURN is correct that applicants' proposal allows GTE California to take merger cost savings associated with a currently less competitive service (i.e., basic exchange), and use them to lower its prices for more competitive services (e.g., toll). This is unreasonable, particularly since applicants have some pricing flexibility for Category 2 services. For example, applicants could—to the extent within the price band and as allowed by competition—offset a surcredit on Category 2 services by increasing rates the same amount. As such, customers would get no benefit. On balance, residential basic access rates should be included in the surcredit billing base to increase the likelihood that benefits are returned to ratepayers.

We also agree with TURN that the merger will reduce costs for all services, including residential basic exchange service. An allocation that includes residential basic exchange service maintains the same relationship between rates, and does not harm residential customers by a shift of economies from residential to business customers.

Applicants contend that the basic residential rate is already set below cost and reducing it further will distort the rate structure. TURN contends the rate is not below cost. Whether it is or is not below cost, the surcredit will not be sufficiently large to distort the final rate. Moreover, as implemented here, it will promote equity by maintaining the same relationship between residential and business rates.

TURN is also correct that we included the residential basic exchange rate in the merger surcredit adopted in the SBC/Telesis decision. No party offers sufficiently compelling reasons to do otherwise here.

Applicants and ORA contend that including basic residential access charges in the base over which the surcredit is allocated will pose problems for calculating the ULTS and CHCF-B funds. To the contrary, Pacific's surcredit applies to all Category 1 and 2 services, including residential basic exchange service. As TURN points out, the surcredit has not complicated Pacific's CHCF-B and ULTS funds or funding.

3.3.7.2. Levelized Revenue Reduction and Surcredit

We adopt applicants' proposal to use a levelized annual revenue reduction (i.e., the same amount of revenue reduction each year) rather than using a discount rate to increase the amount of the revenue reduction each year as we did in the SBC/Telesis merger decision. No party opposes applicants' proposal here, and either method returns the same amount of money to ratepayers on a net present value basis. We also adopt applicants' unopposed proposal to recalculate the billing base each year.

Applicants propose that the revenue reduction be implemented through a surcredit initiated by the filing of an advice letter within 30 days after merger closing. We decline to adopt this recommendation. Rather, applicants should apply the revenue reduction in their first October 1 new regulatory framework price cap advice letter filing made after consummation of the merger, and in each subsequent price cap advice letter for a total of five years. Including the revenue reduction with price cap filings will reduce customer confusion and frustration that can occur with multiple rate changes, will promote administrative convenience for applicants and the Commission, and is consistent with the approach used in the SBC/Telesis merger decision.

We also take account of the timing of the revenue reductions here, just as we did in the SBC/Telesis merger. That is, the net present value of the stream of revenue reductions reflects the fact that the reductions do not begin immediately with merger consummation, but are tied to price cap advice letters and subsequent rate adjustments. As such, the levelized annual revenue reduction is $19.0 million per year for five years based on the first revenue reduction being included in the price cap advice letter filed October 1, 2000, with the first rate adjustment occurring in 2001. (See Attachment B.)

Each advice letter should specify, among other things, the billing base for the purpose of the surcredit. The billing base should reflect current local, toll and access service revenues at the time of the price cap filing, and include both the amount of the CHCF-B fund and annual total revenues from monthly residential exchange service access charges.

The record here shows that the initial billing base, including residential basic exchange service, is about $2 billion. The initial surcredit would, therefore, be about 0.950%.[44] On the average residential bill of $33.18 per month, the initial surcredit will be $0.32 per month. On the average business bill of $49.30 per month, the initial surcredit will be $0.47 per month.

4. COMPETITION

Before authorizing the proposed merger, the Commission must find that applicants' proposal does not adversely affect competition. (§ 854(b)(3).) To assist with its consideration, the Commission must request an advisory opinion from the Attorney General. (Id.) The Attorney General is to advise us whether competition will be adversely affected by the merger, and, if so, what mitigation measures might be adopted to avoid this result. While the Attorney General's opinion is not controlling, it is entitled to "great weight."[45]

Applicants claim that the proposed merger will have no adverse effects on competition and that it will, in fact, have substantial pro-competitive effects. Public Advocates contend that the CCA promotes access and competition in under-served communities.

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[44] 19.0 over 2,000 is 0.00950, or 0.950%.

[45] D.97-03-067, 71 CPUC2d 351, 420, footnote 31. Also see Attorney General's Opinion, page 3, citing Moore v. Panish (1982) 32 Cal.3d 535, 544, and Farron v. City and County of San Francisco, (1989) 216 Cal.App.3d 1071.

ORA asserts that the impact of the proposed merger on competition is uncertain since applicants have provided insufficient evidence for the Commission to make a finding. AT&T, MCI, and Sprint argue that the proposed merger will harm competition.

The Attorney General filed his advisory opinion on September 15, 1999, approximately two weeks after the filing of opening briefs. On September 24, 1999, parties addressed the Attorney General's Opinion in their reply briefs.

The Attorney General concludes that the merger:

> "...will not adversely affect competition within the meaning of section 854(b)(3)." (Opinion of the Attorney General on Competitive Effects of Proposed Merger Between GTE Corporation and Bell Atlantic Corporation, September 15, 1999, unnumbered page preceding Outline of Analysis.)

Further, the Attorney General says:

> "We conclude that this merger will not adversely affect competition within California telecommunications markets. The record contains no evidence that Bell Atlantic would have entered California markets in the absence of this merger. Moreover, AT&T, MCIWorldCom, Sprint, and other well-financed companies [e.g., SBC , and perhaps U.S. West, Bell South, ICG, Nextlink, Electric Lightwave, other inter-exchange carriers, competitive exchange carriers and cable companies [46]] do plan to provide service in major markets where entry is at least theoretically profitable. Entry by these and other firms has already reduced both prices and concentration levels within the intraLATA toll and direct access markets.
>
> "We also conclude that the merger by itself will not enhance anticompetitive cross-subsidization opportunities." (Id., page 26.)

[46] See Attorney General Opinion, pages 15-16, and footnote 85.

We agree with applicants and the Attorney General that the proposed merger will not adversely affect competition.

4.1. Scope of Analysis

We are guided by federal antitrust law (e.g., Section 7 of the Clayton Act), but we do not need to find a specific violation of that law in order to deny a proposed merger. (See D.97-03-067, 71 CPUC2d 351, 379; also see D.91-05-028, 40 CPUC2d 159, 182.) Rather, under § 854, we may disapprove a merger the impacts of which are harmful, but less than "substantial" under the Clayton Act. (D.97-03-067, 71 CPUC2d 351, 379.) We may also rely on the body of common law regarding competition that existed before 1989, when the effect on competition standard was codified for utilities in § 854. (Id.) [47]

Further, whether or not applicants have market power now, applicants' existing level of market power is the base from which our competitive analysis begins. That is, the inquiry here focuses on specific evidence as to whether or not this proposed merger increases or otherwise enhances that market power. Moreover, as we said in the SBC/Telesis decision, we do not find that a merger in itself—absent specific evidence to the contrary—adversely affects competition simply by making a large and strong company larger and stronger. (Id.)

We address competition in the same order as have parties. We first consider whether or not there are pro-competitive effects. Second, we review whether or not the proposed merger will adversely affect competition. Within this second assessment, we assess relevant markets, whether Bell Atlantic is an actual competitor, whether Bell Atlantic is an actual potential competitor, and other

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[47] AT&T and MCI also point out that, independent of Section 854, the Commission has an obligation to assess the antitrust impacts of matters we consider. (*See Northern California Power Agency v. Public Utilities Commission* (1971) 5 Cal. 3d 370, 379-380.)

possible adverse effects, such as price discrimination, locking up the large business market, non-price discrimination, and a decrease in the amount of benchmarking information. Third, we evaluate the balancing of pro-competitive and anti-competitive effects. Finally, we consider the weight to give the Opinion of the Attorney General based on comments of parties in their reply briefs.

4.2. Pro-competitive Effects

Whether or not there are pro-competitive effects, applicants must prove by a preponderance of the evidence that the proposed merger does not adversely affect competition, and the Commission must find this to be the case. (§§ 854(e) and 854(b)(3).) Nonetheless, parties first address the pro-competitive effects, which we also consider first, and which assists in our weighing the arguments for and against the merger.

We are convinced by applicants that the merger will have pro-competitive effects, and will provide important benefits to California. For example, the merger will allow GTE and Bell Atlantic to compete more effectively in a changing telecommunications marketplace, where barriers which have divided markets by geographic and product lines are changing.

Merger opponents contend that the merger will heighten applicants' existing incentives and abilities to disadvantage rivals. When rivals are harmed, opponents say competition is harmed, and California consumers are harmed. For the reasons explained below, we find that the rivalry will stimulate competition, and applicants will not be advantaged compared to any potential competitor.

Indeed, many competitors of GTE and Bell Atlantic have positioned themselves to compete in this new, changing environment by merging. These merged competitors include (1) SBC/Telesis/SNET/Ameritech,
(2) AT&T/TCG/TCI/British Telecom/MediaOne, and
(3) MCI/WorldCom/MFS/UUNet. These companies have recognized that their

ability to be future first tier, sophisticated telecommunications providers depends on a level of financial and technological resources and economies of scale that can best be achieved by merging with other companies, thereby providing important and valuable synergies. GTE and Bell Atlantic have reached the same conclusion.

ORA argues that other merging companies have promised pro-competitive effects from their mergers that have not materialized. For example, ORA says the 1997 SBC/Telesis merger has not produced any effective entry in any out-of-franchise area, nor has it resulted in the full elimination of barriers to entry that would facilitate the development of effective competition.

We agree with ORA that competition may not yet have developed as far and as fast as we would all like. Nonetheless, we think that it continues to develop, and we continue to address issues that will facilitate competition in appropriate proceedings (e.g., operations support systems (OSS), open architecture and network access development (OANAD), number portability, arbitrations of interconnection agreements). Overall, this merger will facilitate competition in at least four areas: products and services, out-of-franchise, long distance and data, and internet.

4.2.1. Products and Services

The merger will increase GTE's ability to offer innovative, competitively priced products and services in California. First, the merged entity will have greater financial resources than GTE has today, which will permit greater investment in new products and services. Second, the increased scale and scope of the merged entity will result in significant savings (only part of which are returned to ratepayers), which in turn will enable the merged firm to invest in new products and services to a greater degree than GTE could alone. Third, the merger will give GTE access to Bell Atlantic's technical and marketing expertise, and will enable GTE to adopt Bell Atlantic's best practices in those areas.

The benefits will be both direct and indirect. Consumers will benefit directly when they use innovative products and services at competitive prices resulting from the merger. This innovation will also benefit customers indirectly, as competitors respond to innovation with innovations of their own.

ORA, AT&T, MCI, and Sprint recommend disregarding this alleged benefit. AT&T contends, for example that applicants do not identify any specific product or service that the merger will allow them to develop and offer that GTE could not pursue on its own.

We are not convinced. By their very nature these items are innovative, and have not yet been developed. Moreover, it would be premature for applicants now to identify products and services that GTE might develop and offer with Bell Atlantic only after they are merged. Further, even if these items are known, it could be unwise to announce them now before discussing optimal marketing with the new merged marketing department, and enjoying any competitive advantage that might accrue.

AT&T, MCI and Sprint contend that, contrary to applicants' claim, a bigger company will not necessarily be more innovative, and that many great innovations come from small companies. Even if they are right, this does not prove that such innovations have not, and will not, also come from large companies.

Sprint asserts that separate firms might each have generated valuable innovations, and that elimination of duplicative research expenditures may actually reduce innovative output. We are not persuaded. Sprint's argument is no more than speculation. Moreover, without specific information to the contrary, it is generally true that duplicative expenditures are wasteful, not productive. Elimination or continuation of "duplicative" research expenditures by the merged company is a decision the new management can make based on data regarding innovative output. Finally, we have no evidence here that this merger—even if it results in reduced expenditures for research—creates such a reduction in, or concentration of, research effort throughout California or the United States that Sprint's argument merits a different outcome for this application.

4.2.2. Competition Out-of-Franchise

The merger will promote competition by increasing GTE's ability to compete out-of-franchise, particularly in Pacific's territory.[48] Prior to the merger, GTE did not have the ability to compete broadly and effectively out-of-franchise. GTE attempted to do so by forming GTECC in 1996 to operate as a CLEC. GTECC's success has been limited, and GTECC has scaled back its future goals.

This merger, however, will enable GTE to compete more effectively out-of-franchise because it will (1) increase GTE's ability to compete for large business customers, (2) give GTE the ability to develop a nationally recognized brand, (3) increase GTE's financial resources, and (4) reduce GTE's costs. In support of the merger and this concept of increased out-of-franchise competition, GTE's chairman, Charles R. Lee, appeared before the United States Senate on September 15, 1998. He there testified that the merged company intends to enter 21 out-of-franchise markets within 18 months of the merger's consummation, including Pacific's service areas in San Francisco, Los Angeles and San Diego.

ORA and others point out that applicants here testified they do not consider the pledge to enter out-of-franchise markets a legal commitment. Rather, applicants only state their plans are a public intention and moral commitment. In fact, applicants oppose any condition placed on merger approval relative to this intention (e.g., financial compensation to ratepayers if the intention is not fulfilled). AT&T says applicants' intentions are empty promises. ORA and AT&T suggest

[48] Out-of-franchise here means outside of the franchise service area of GTE.

that no weight be given to applicants' out-of-franchise intentions as being pro-competitive.

We are disappointed that applicants do not make a legal commitment to serve San Francisco, Los Angeles and San Diego within 18 months of merger consummation. Certainly a binding commitment would make the pro-competitive claim much more credible. Nonetheless, we do not dismiss this benefit of the merger.

For example, whether or not a legal commitment, applicants' witness Atwood testified under oath here that it is a "public intention and moral commitment of both Mr. Lee [GTE's chairman and chief executive officer] and Mr. Seidenberg [Bell Atlantic's vice chairman and chief executive officer]." (2 Tr. 182: 23-24.) We expect applicants to honor their intention and commitment, and believe applicants will do so.[49]

Competition out-of-franchise is complex for many reasons, as GTECC's experience shows. This merger, however, will enable GTE to compete more effectively out-of-franchise by increasing GTE's ability to compete for large business customers, giving GTE the ability to develop a nationally recognized brand, increasing GTE's financial resources, and reducing GTE's costs. These are further reasons to apply some weight to this benefit, and to expect applicants to honor their commitment.

ORA cites a Cambridge Strategic Management Group (Cambridge) report commissioned by GTE. ORA says that report shows applicants are unlikely to compete out-of-franchise. In response, applicants explain that they rejected the financial projections in the Cambridge study. Rather, applicants assert that they

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[49] We also recognize that applicants' plans must reflect relevant market conditions at the time specific decisions are made.

prepared a joint venture business case and came to different conclusions on the profitability of entering out-of-franchise areas. We accept the testimony of applicants' witnesses that "the merged company fully intends to compete for as many residential customers as it can in as short a timeframe as possible." (Applicants' Reply Brief, pages 40-41, citing testimony of applicants' witnesses Kissell and Teece.[50])

ORA and others say the merged company might not compete for residential customers, and even if it does, will compete for only a small percentage. We are convinced by applicants, however, that one valid business strategy (although not necessarily the only one a firm might adopt) is to first develop business customers, and then expand into residential service. Moreover, a valid business strategy may be to compete for residential customers gradually rather than on a vast scale all at once. Further, market effects happen at the margin. Serving only a small percentage can still have a significant effect on the overall market. Finally, we are convinced by applicants that they in fact intend to compete for residential customers to the fullest extent feasible as soon as possible.

AT&T and MCI argue that Bell Atlantic has here contended that it is not a potential competitor in Pacific's market because it has no capability to compete in California, while GTECC's experience shows GTE cannot compete out-of-franchise on its own. AT&T and MCI conclude that GTE cannot reasonably rely on Bell Atlantic for its ability to compete out-of-franchise. We disagree. AT&T and MCI miss the nature of synergies. Synergies allow two companies together to do what each cannot do alone.

[50] For example, Kissell states that "the merged company is committed to serving residential customers as part of its expansion out-of-franchise." (Exhibit 5, page 13: 9-10.)

Sprint and ORA cite comments made by GTE that GTE plans to compete on its own out-of-franchise. To the contrary, as applicants point out, those comments were made before GTE made its decision to scale back GTECC's efforts out-of-franchise. Further, Sprint cites comments of GTE's chairman that GTE is exceedingly capable of competing out-of-franchise. Those comments, however, were made in October 1998, three months after the merger announcement. It is unreasonable to conclude that GTE's chairman made those comments without consideration of the pending merger.

Thus, we do not dismiss this benefit. Applicants should, however, serve a report on the Director of the Telecommunications Division, with copies on the service list to this proceeding, within 20 months of consummation of the merger regarding this merger benefit. The report should address applicants' success at meeting their intention and commitment to serve markets in San Francisco, Los Angeles and San Diego within 18 months of consummation of the merger. If the goal has not been met, the report should explain the plans to meet this intention and commitment, or, if the plans have changed, should explain the reasons for changing the plan.

4.2.3. Long Distance and Data Markets

Applicants also claim that the merger will foster competition in the long distance and data markets by enabling GTE to expand its Global Network Infrastructure (GNI).[51] GTE says it cannot achieve sufficient traffic on its own to develop a full-fledged, national network by selling only to its own dispersed

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[51] GTE says its Global Network Infrastructure is its internet backbone network. GTE plans to migrate some of its long distance traffic to its GNI. When fully developed, applicants contend the GNI "will create another facilities-based long distance carrier to rival the only three companies who have long distance networks that are truly national in reach: AT&T, MCI WorldCom, and Sprint." (Exhibit 1, Chapter 1, page 11.)

customer base. According to applicants, Bell Atlantic's traffic will provide the necessary scale to deploy the GNI sooner, and into more markets than otherwise planned (including an additional 11 cities in 2001). Moreover, applicants claim that the economies of scale resulting from the addition of Bell Atlantic's traffic on the GNI will reduce costs and make applicants a more effective competitor in the long distance and data markets.

Sprint argues that there is a substantial likelihood that GTE can fill its GNI capacity by seeking its own retail customers, or selling wholesale services. This may be true. This does not negate the desirability of GTE's plan to more fully utilize the GNI by adding Bell Atlantic traffic, nor does it show that GTE's plan to use Bell Atlantic traffic is unwise. Applicants have not said, for example, that they will not seek retail and wholesale sales in addition to Bell Atlantic's traffic. We find nothing that invalidates applicants' judgment that a reasonable way to accomplish this goal is by adding Bell Atlantic's traffic via the merger.

AT&T and MCI argue that the benefits of GNI expansion are illusory. They contend that long distance and data services are already highly competitive, and the addition of applicants will produce no incremental benefit. We are not persuaded that adding another facilities-based carrier has no benefit, even if it is true that long distance and data services are already highly competitive. Rather, the addition of another carrier always adds to competition, notwithstanding diminishing returns as the number increases.

More serious, however, is the concern that Bell Atlantic's long distance traffic originating within Bell Atlantic's service area might not be able to be carried over the GNI until Bell Atlantic receives approval from the FCC to transmit long distance traffic generated within its service area under § 271 of the Act. In contrast, GTE can now carry long distance traffic. The merger might in fact slow GTE's use of the GNI. This concern tempers the weight we give this benefit. Nonetheless, no merger opponent presents clear, specific evidence on the development of the GNI with and without the merger. On balance, we are convinced by applicants that the merger will foster competition in the long distance and data markets by enabling GTE to expand its GNI in ways that it otherwise would not.[52]

4.2.4. Internet Services

Finally, the merger will increase competition in the market for internet services. GTE's internet services market share is well below that of MCI, Cable & Wireless (MCI's successor) and Sprint. The merger will make GTE a more potent competitor in this market by creating the opportunity to (1) add Bell Atlantic's customer base to its own, thereby expanding the data and internet traffic on GTE's internet backbone network, (2) increase the number of valuable web sites and customers connected to GTE's network, and (3) accelerate the transition of GTE's backbone to the GNI. California businesses and consumers will benefit from this increased competition.

AT&T and MCI argue that applicants are attempting to dominate the market for internet services and, rather than increasing the level of competition, approval of the proposed merger will actually decrease competition. We are not convinced by any evidence here that the market for internet services is dangerously concentrated, or that the proposed merger will decrease competition for internet

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[52] We decline to condition merger approval on GTE satisfying the 14-point checklist in § 271 of the Act. Nonetheless, Bell Atlantic's need to obtain Act § 271 authority, and the effect that may have on GTE's ability to fully use its GNI, may have nearly the same effect as placing a § 271 condition on the merger. At the same time, we have no evidence to conclude that this will delay GTE's expansion of the GNI. In fact, the objective of the merged company to expand and fully use the GNI may provide further incentive for Bell Atlantic to more quickly satisfy the Act § 271 checklist than it might otherwise have. With the increased financial resources of the merged company, this might result in a more rapid expansion of the GNI than without the merger.

services. For example, the largest single provider of internet services (America Online) has less than half of the internet market, and there are dozens of internet service providers (ISPs) competing for market share. Moreover, no evidence presented here shows that internet backbone facilities are dangerously concentrated.

AT&T and MCI say that once merged, applicants will control one-third of the country's access lines. Applicants will be able to exploit this bottleneck monopoly to endanger competition among ISPs, according to AT&T and MCI. We are not convinced. ILECs now control much more than 33% of the access lines within their service territories, but this does not adversely affect ISP competition. For example, America Online is neither an ILEC nor a CLEC, but has a large market share.

Neither are we convinced that the merger will produce a firm that will be able to dominate the internet market, nor that applicants will be able to successfully tie their products and services to dominate the internet market. For example, cable access to the internet is being deployed, and other alternatives (e.g., wireless) are being developed and deployed. Whatever ability applicants might theoretically have to tie products and services because they control the local loop is in jeopardy.

Moreover, using price discounts to tie products and services can be a form of healthy competition when they meet market demand and are cost-justified. We have no more than speculation that any possible future price discounts would not be cost-based, or would in some other way be unlawful. We will neither deny nor condition merger approval on such speculation.

There is no basis to conclude that the merger will endanger competition among ISPs. The Attorney General agrees. (Attorney General Opinion, pages 22-23.)

4.3. Proposed Merger Will Not Adversely Affect Competition

Applicants must prove by a preponderance of the evidence that the proposed merger does not adversely affect competition. (§§ 854(e) and 854(b)(3).) Moreover, we must find that the proposed merger does not adversely affect competition. (§ 854(b)(3).) We conclude that applicants have met their burden of proof, and we make the necessary finding.

In support of its showing, applicants point out that the United States Department of Justice (DOJ) has concluded that the merger poses no antitrust concerns in any geographic or product market, with the exception of some overlapping wireless properties outside California which applicants have agreed to sell. We concur with applicants that this is significant evidence we may consider here.[53]

Moreover, as applicants point out, merger opponents present arguments regarding competition that are not unique to California. Rather, opponents' arguments relate to concerns about anti-competitive effects which, to the extent the merger would have such effects, would take place around the country. The DOJ was in a position to assess these concerns. As applicants say, the:

> "DOJ is responsible for determining if a merger would have an adverse competitive effect 'in any line of commerce...in any section of the country...' under Section 7 of the Clayton Act. The DOJ's determination therefore provides powerful evidence that the merger will not harm competition anywhere in the country, including California." (Applicants' Opening Brief, page 117, citing 15 U.S.C. § 18.)

[53] AT&T and MCI criticize applicants' reliance on the DOJ's determination, saying applicants did not present the DOJ's determination as evidence. To the contrary, applicants offered Exhibit 2, which is the DOJ stipulation and proposed final judgment.

We agree. At the same time, ORA correctly observes that our authority and responsibility go beyond those of the DOJ, and we exercise a broader review of the relevant markets and proposed transaction. Nonetheless, the DOJ's finding is a significant consideration.

4.3.1. Relevant Markets

We must look at each relevant market to consider whether the proposed merger adversely affects competition. Parties do not agree on the relevant markets.

Applicants contend that the relevant markets are local exchange, intraLATA toll, interLATA toll, data/internet, and wireless markets all within California.[54] Public Advocates agree with applicants, pointing out that the relevant markets include California's low-income, minority, limited English-speaking and disability communities.

ORA asserts that the relevant product markets are local exchange, digital subscriber line (DSL), internet, intraLATA toll, interLATA toll and switched access in California and marketed to out-of-state locations of large business

[54] These markets can be more fully understood with the following information. A telephone company's service area is divided into exchanges. Each exchange has a single point designated as the rate center. Calls originating and terminating within an exchange are local, toll-free calls. Calls between exchanges are local, toll-free calls when the rate centers are within 12 miles of each other. Calls between exchanges are toll calls when the rate centers are more than 12 miles from one another (except in a few cases where there is special extended area service). Local exchange service refers to calls within or between exchanges that are local, toll-free calls. California is divided into 10 Local Access and Transport Areas (LATAs) as a result of the divestiture of AT&T in 1984. Each LATA contains numerous exchanges. IntraLATA toll refers to calls other than local exchange calls that originate and terminate within a single LATA. This is sometimes referred to as the local toll market. InterLATA toll refers to calls between LATAs. This is generally referred to as the long-distance market. Internet is an international telecommunications system connecting local computers. Wireless is service by cellular carriers.

customers in California.[55] ORA says the relevant geographic market includes the national market of integrated telecommunications services.

AT&T and MCI claim that the relevant product markets are local services, xDSL, internet, long-distance and switched access services in California, and the market for large, national business customers. Relevant markets include both retail and wholesale services, according to AT&T and MCI. The most important and relevant market, according to AT&T and MCI, is the market that is the focus of the transaction: the national business market. AT&T and MCI assert applicants make clear that this is their target market, consisting of large business customers with multiple locations around the country. In contrast, Sprint does not disagree with variously identified markets, but focuses its analysis on the California local exchange market.

The Attorney General says that, in order to avoid speculation, he limits the product market to the range of competitive services currently offered by both merging companies. Further, the Attorney General says he accepts California as the relevant geographic market because, according to the Attorney General, this is a "conglomerate" merger between non-competitors.[56] Finally, the Attorney General rejects suggestions that local services provided outside California are part of any relevant market for this merger analysis.

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[55] Digital Subscriber Line (DSL) refers to special digital transmission, either by synchronous or asynchronous means, with xDSL referring to either type. Switched access refers to a service local carriers provide to other carriers, wherein the local carrier makes its facilities available for the transport and termination of toll calls.

[56] Mergers can be classified as horizontal, vertical or conglomerate. Horizontal mergers are those in which rivals in the same market merge. Vertical mergers are those between firms with a potential or actual buyer-seller relationship. Mergers that are neither horizontal nor vertical are conglomerate mergers. (Exhibit 167, page 23.)

We think the parties' differences largely reflect a local, state, or national approach to defining the market. There is no question that the merger must be examined to see if it affects retail and wholesale markets for local exchange, intraLATA toll, interLATA toll, switched access, xDSL, internet, and wireless markets within California. California, after all, is our jurisdiction. Moreover, there is no question that applicants propose and support the merger on the basis that they plan to offer a full package of wireline, wireless, long distance and data services to customers nationally, and compete with other national providers. Therefore, we must also consider the national market. Under each market viewpoint, however, we conclude that the merger does not adversely affect competition.

4.3.1.1. Local and State Markets

Both GTE and Bell Atlantic offer a variety of retail and wholesale services, including local exchange, toll, switched access, xDSL, internet, and wireless. They do not simultaneously offer them within California, however, with the exception of 440 California long distance customers of Bell Atlantic. Rather, GTE offers these services locally and statewide within California, while Bell Atlantic does not (except for the noted minor number of long distance customers). We agree when the Attorney General concludes:

> "...they do not compete in California. Furthermore, there is no evidence that Bell Atlantic has any current effect upon GTE operations within California, or that Bell Atlantic would enter any California market served by GTE in the absence of the merger." (Attorney General Opinion, page 10.)

Thus, the proposed merger will not adversely affect competition in the local and state markets.

4.3.1.2. National Market

ORA contends that the merger will increase concentration in the national market, as measured by the Herfindahl-Hirschman Index (HHI), from 1621 to 2677.[57] ORA concludes that this is an anti-competitive outcome. We are not convinced for several reasons.

First, the DOJ has withdrawn its opposition to the merger. We think the DOJ is capable of the same type of concentration analysis performed by ORA, using the HHI index. We believe that the DOJ satisfactorily performed its job, and did not reach the same conclusion as ORA. We have confidence in the DOJ's conclusion.

ORA argues otherwise. ORA says that the DOJ's analysis is static and narrow, and does not encompass the dynamic and broader view of the impact on competition in the local market that must be considered by this Commission. For example, ORA says the DOJ's analysis "does not address critical questions such as the impact of the proposed merger on the likelihood that concentration in the local market will begin to diminish." (ORA Opening Brief, page 33.)

As discussed more below, ORA's analysis mixes several markets. Nonetheless, there is no dispute that GTE currently dominates the local market as the ILEC.[58] As ORA says, this merger will not increase the local market

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[57] The HHI is used by the DOJ and others to measure market concentration. The HHI of an industry with one seller is 10,000. This is computed as the market share (measured by the firm's percentage of total industry sales) of the single seller (100%, or 1.0) times 100, with the result squared. The HHI for an industry of four sellers each with 25% market share would be 2,500. This is computed by multiplying 25% (or 0.25) times 100, squaring the result, and adding each of the four results (i.e., adding 25 squared four times). There are three categories of market concentration: unconcentrated (HHI below 1000), moderately concentrated (HHI between 1000 and 1800), and highly concentrated (HHI above 1800). (Exhibit 167, page 27.)

[58] GTEC's share of the local market is approximately 99%. (Exhibit 167, page 29.)

concentration index. (Exhibit 167, page 29.) We do not view a decrease in concentration as undesirable.

The dynamic consideration is that local markets have the opportunity to become less (not more) concentrated as a result of the 1996 Telecommunications Act, and our implementation of the Act (e.g., arbitrations of interconnection agreements). The merger by itself will not change GTE's position in the local market. That is, GTE California's market share in California will remain exactly the same before and after the merger, other things held constant. Dynamically, however, the merger will increase competition to the extent the merger results in GTE/Bell Atlantic competing out-of-franchise (e.g., in Pacific's territory) and other ILECs responding in kind (e.g., Pacific competing in GTE/Bell Atlantic's territory). We see this as a likely response by ILECs. To the extent there is a national market, this dynamic effect will increase competition in that market.

Further, in the first quarter of 1998, net business line additions for CLECs as a group exceeded those of RBOCs for the first time. This is only a start, but we are not convinced by any evidence or testimony here that this trend will reverse. Again, to the extent there is a national market, this trend will further increase competition in that market.

Second, ORA's analysis is incomplete. ORA's analysis assumes that major ILECs are the only potential entrants into the local market. To the contrary, this approach fails to include inter-exchange carriers (IECs), competitive local exchange carriers (CLECs), and alternative suppliers (e.g., wireless).

ORA, in fact, accepts that present and potential CLECs (e.g., AT&T, MCI) should be included in the analysis, but claims that their market shares are so small at present that they would not materially affect the HHI calculation. Even if CLEC market shares are small at present, however, this is not the end of the analysis. An analysis based on the ILECs' current market shares is static, not dynamic.

A dynamic analysis must recognize that the local market is changing. As discussed above, local market competition is, if anything, increasing. Existing market shares fail to capture these dynamic possibilities.

Third, the national market ORA seeks to assess by examining local market shares of ILECs mixes markets, and is confusing. That is, there is currently no national market of bundled services (e.g., local, intraLATA, interLATA, wireless, internet, cable).[59] ORA seeks to measure a market that does not now exist, but that is a future market, by examining current market shares. To the extent this market does not now exist, the HHI is zero, not 1621 or 2677. If a national, bundled market develops, the market shares at that time are unlikely to be the same as those represented by ORA now (i.e., market shares calculated based on existing ILEC access lines summed to represent a national market).

Moreover, ORA's analysis mixes markets and is confusing because, as applicants point out, the local exchange customer in one ILEC's territory cannot change to another ILEC operating in a different territory. Local exchange services offered by one ILEC are not part of the same market as local exchange services offered by another ILEC.

The HHI for GTE California in the local market is at least 9800, according to ORA. The merger by itself will not change that, other things held

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[59] For example, in its criticism of the DOJ's analysis, ORA says: "using the static model upon which the DOJ must rely, the bundled services market is irrelevant because it does not yet exist." (ORA Opening Brief, page 34.) ORA also says it is appropriate for the Commission to "undertake a dynamic analysis that not only addresses the structure of the market as it exists today, i.e., a market that does not yet encompass a national bundled services market..." (ORA Reply Brief, page 46.)

constant. Moreover, the merger by itself will not change the ability of CLECs to enter or compete in local markets, nor to form national alliances and national customer bases. A complete analysis must include the CLECs in the local markets, and the dynamics of change in the local markets, not existing market shares of ILECs who may or may not be CLECs in each other's territory. Thus, we are not convinced by ORA's analysis that the national market—to the extent it exists or will exist—is not competitive, or that the merger will adversely affect competition.

4.3.1.3. National Business Market

Neither are we persuaded by the analysis of AT&T and MCI. AT&T and MCI postulate a national business market for packaged services. This is based on their conclusion that applicants intend, as a result of the merger, to target large business customers with operations in numerous locations and many states for packaged services. This market does not now exist, however.[60] Nonetheless, AT&T and MCI seek to measure a hypothetical market that does not now exist by examining current market shares. This mixes markets and is confusing, just as is ORA's analysis.

AT&T and MCI assert that the most useful measure of a carrier's position in this national business market is the number of multi-line business access lines. Using this approach, they conclude that the merger will increase concentration, with SBC/Ameritech controlling 37.6% of the market, and GTE/Bell Atlantic controlling 36.1% of the market. That is, two firms, according to AT&T and MCI, will control 73.7% of the market, producing an anti-competitive result.

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[60] AT&T and MCI witness Gillan says "if we accept the premise of a national business market." (Exhibit 108, page 8, lines 9-10; emphasis added.) He later says "...if in fact there *are* national business customers..." (Exhibit 108, page 35 (lines 13-14), emphasis in original.) The Attorney General calls it an "alleged 'national business market'" and "this hypothesized market." (Attorney General Opinion, page 18.)

Even if it makes sense to use current shares to measure a market that does not exist (a proposition which we reject), this approach fails to separately identify business customers with a need and desire for national coverage from those without such need and desire. For example, many businesses are local, but may, at the same time, have more than one access line. These businesses do not necessarily have an interest in a national market. Even businesses with more than one local office and multiple access lines do not necessarily need and desire national business service.[61]

Further, the AT&T and MCI analysis assumes that the carrier controlling the customer's access line is in the best position to provide that customer with a full range of services, including national services. What this analysis misses is that the merger by itself will not change who currently controls the access line, or who will control it in the future. The efforts to open access will not be affected by this merger. That is, the requirements of the Act are not repealed by this merger, and we are not convinced that the merger will hamper our efforts to implement the Act.

The Attorney General characterizes the AT&T and MCI theory as based on the idea that the power of the ILEC is related to the number of exchanges it serves. Thus, the bigger "footprint" of the merged firm allegedly increases the leverage of the ILEC over competitive markets. We agree with the Attorney General, however, when he concludes that AT&T and MCI did not provide

[61] The AT&T and MCI witness says if he used all business lines (not just multi-line business customers) the concentration would be even higher. This also misses the point, however, since the need is to more accurately focus the analysis on customers requiring national coverage, not all business customers.

compelling evidence of the supposed relationship between footprint size and market power. (Attorney General Opinion, page 19.)

Moreover, opponents' analysis is based on current access lines and is, in that sense, static. It misses the dynamic competition that is occurring in the business market by competitive access providers (CAPs), CLECs, and providers with alternative options (e.g., wireless, fiber optic metropolitan area networks, cable). Competitors for business customers are increasingly able to bypass GTE's system entirely.

For example, testimony here shows that large, national business customers are particularly able to shop among telecommunications providers. Opponents themselves agree that "local competition is practical today" in the large business market. (AT&T and MCI Opening Brief, page 11.) Even if applicants seek to monopolize this national business market, as opponents claim, effective local competition will be a countervailing force.

Further, opponents' analysis is essentially composed of the number of business lines in each ILEC's territory. This shows that there are more multi-line business access lines in Bell Atlantic's territory than others, but says nothing about the degree of market power or concentration in the hypothesized national business market.

A complete assessment of market dominance and competitive position must examine more than just access lines. Revenue and profit, not just access lines, are important to competition and a firm's place in the market. For example the top 1% of Bell Atlantic's business customers in Pennsylvania generate 55% of its business revenues. Loss of this 1% of business customers would be more than a 1% loss in market share.

Finally, as we said above, we believe that the DOJ satisfactorily performed its job, and did not reach the same conclusion as AT&T and MCI. We are not persuaded by AT&T and MCI that the national business market—to the extent it exists or will exist—is not competitive, or that the merger will adversely affect competition.

4.3.2. Elimination of Actual Competitor

The proposed merger could adversely affect competition if it eliminates an actual competitor in any relevant market. With the exception of 440 long distance customers, no party claims Bell Atlantic is an actual competitor of GTE in California. No party asserts the 440 long distance customers represent a significant base of actual competition, or that elimination of Bell Atlantic as an actual competitor in the long distance market would be anything other than competitively insignificant.

4.3.3. Elimination of Actual Potential Competitor

The proposed merger could also adversely affect competition if it eliminates an actual potential competitor in any relevant market. An actual potential competitor is a firm that does not currently compete in the relevant market but which would enter sometime in the near future, either independently or in combination with another entity. The combination with another utility is called a toehold acquisition. If the actual potential competitor entrant merges with a significant incumbent firm, the incentives disappear that it would otherwise have to enter the market independently or by toehold acquisition. In that case, the market loses the amount of new competition that the potential competitor would have generated. (D.97-03-067, 71 CPUC2d 351, 383.)

We have held that to prove a loss of actual potential competition, one must establish that: (1) the relevant market is concentrated; (2) but for the merger, the acquiring firm would likely have entered the market in the near future either on its own or by toehold acquisition; (3) there must be few other potential entrants with comparable advantages; and (4) such market entry would carry substantial likelihood of ultimately producing deconcentration of the market or other significant pro-competitive effects.[62]

Applicants contend that Bell Atlantic is not an actual potential competitor to GTE California. The Attorney General agrees. ORA, AT&T, MCI and Sprint disagree.

Sprint also says that the telecommunications market is characterized by still evolving business strategies of potential competitors. Sprint asserts that evolving strategies may require us to use greater flexibility in applying our standards for determining an actual potential competitor. Sprint contends that the risk of eliminating an actual potential competitor—even if the potential entrant may not meet a strict application of our criteria—must be weighed against the benefits of the merger.

Using our criteria for this determination, we find that Bell Atlantic is not an actual potential competitor. We also weigh the risks and benefits, and reach the same conclusion.

4.3.3.1. Is the Relevant Market Concentrated

We address the same markets briefed by the parties.

Local Exchange: There is no dispute that GTE California's local exchange market is now concentrated, with an HHI of about 9800. Applicants encourage us to focus on the trend of this market becoming competitive (e.g., net business additions in the first quarter of 1998 by CLECs exceeding those of RBOCs). We do not ignore this trend, but the market concentration criterion looks more closely at the current concentration level, not toward the future.

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[62] D.97-03-067 (71 CPUC2d 351, 383), citing *Mercantile Texas Corp. v. Board of Governors, Etc.*, 638 F.2d 1255, 1266-1270 (5th Cir. 1981) and *Tenneco, Inc. v. Federal Trade Commission*, 689 F.2d 346, 352 (2nd Cir. 1982).

<u>IntraLATA Toll</u>: There is also no dispute that the intraLATA toll market in California is now reasonably competitive. For example, GTE California's in-region share of this market is less than 50%. Thus, we need not further analyze to any great degree whether Bell Atlantic is an actual potential competitor in California's intraLATA toll market.

<u>National Market</u>: ORA, AT&T and MCI contend that the national markets (both in general, and specifically for business) are already highly concentrated. We are not convinced. First, national markets do not now exist. Second, for the reasons stated above, we reject ORA's, AT&T's and MCI's analyses of concentration in their respective definitions of the national market. To the extent there is any concentration, we agree with the Attorney General that "this merger may actually have the effect of reducing concentration" within this alleged national market. (Attorney General Opinion, page 20.)

4.3.3.2. Would Bell Atlantic Likely Have Entered But for the Proposed Merger

For the entrant firm to be considered an actual potential competitor, the entrant must be "likely" to enter, and there must be a "reasonable probability of entry" in the "near" future. We do not require "clear proof" of entry, but the entry must be more than a possibility. Further, it must be reasonably soon, not just some time in the future. (D.97-03-067, 71 CPUC2d 351, 384-387.)

To avoid speculation, the courts consistently require proof that the acquiring firm "would"—not "could"—enter the target market absent the merger, and that the entry must occur in the "near" future, not the "reasonably foreseeable" future. The courts require that the showing be supported by "substantial evidence." (Attorney General Opinion, page 14.)

We do not have substantial evidence here to demonstrate a reasonable probability that Bell Atlantic would enter GTE California's service area in the near future but for the merger. For example, no documents were offered to show that Bell Atlantic has specific plans to enter any California market absent the merger with GTE. Bell Atlantic has no California network facilities from which to supply service, has virtually no customer base from which to initiate a local offering, has limited marketing presence, has limited brand-name recognition, and has no experience supplying local service in California. Moreover, Bell Atlantic testifies that its experience competing in the long distance market out-of-franchise has been "very sobering" and "dismal," even in areas much closer to Bell Atlantic's franchise territories. (Exhibit 3, pages 26-7.) We agree with the Attorney General's conclusion that "the record contains no evidence that Bell Atlantic would have entered California markets in the absence of this merger." (Attorney General Opinion, page 26.)

ORA contends that "there is a sufficiently plausible possibility" that Bell Atlantic will decide to enter California's local markets, even though "one cannot predict whether future Bell Atlantic management" will decide to do that. (Exhibit 167, page 38, lines 6-9.) A possibility along with the inability to predict future management decisions does not establish by substantial evidence a reasonable probability of entry in the near future.

ORA asserts that "it seems highly improbable that Bell Atlantic would have bypassed California altogether if the acquisition of GTE were not an option." (ORA Opening Brief, page 38.) A witness for AT&T and MCI agrees, saying "it is unlikely that Bell Atlantic would forever ignore...GTE's markets..." and that Bell Atlantic's entry into GTE California's markets "could be sooner than three [years] but certainly within five." (Gillan, Exhibit 108, page 35, lines 14-15; 10 Tr. 1256: 26-27.) Again, this fails to establish by substantial evidence a reasonable probability of entry in the near future.

Sprint says the absence of a business plan to enter California "does not foreclose the material possibility that Bell Atlantic would have entered the California local exchange market absent the Merger." (Sprint Opening Brief, page 12.) Material possibility is not reasonable probability.

Merger opponents argue that the factors which cause Bell Atlantic to be interested in the merger make it likely that Bell Atlantic will seek to enter California in some other way if not by the merger. We reject this argument. Just as we said in the SBC/Telesis merger decision, that analytical approach would necessarily lead to the conclusion that every proposed merger partner would be an actual potential competitor. (D.97-03-067, 71 CPUC2d 351, 385.)

Sprint contends that Bell Atlantic's desire to gain a national presence must not be overlooked, and is a factor that was not present in the SBC/Telesis merger. Bell Atlantic's desire, however, does not demonstrate by substantial evidence a reasonable probability that Bell Atlantic would enter GTE California's service area within the near future absent the merger.

AT&T, MCI, and Sprint suggest the Commission consider applicants' ability and financial capability to enter California, along with Bell Atlantic's incentives to provide services here. For example, Sprint says Bell Atlantic has important assets on which it can rely in building a successful presence in California. Those assets include vast experience as a supplier of local exchange service, first-hand knowledge of the kind of input provisioning of which an ILEC is capable, existing national business customers, and "Bell" brand name recognition.

Just as we found of a similar argument regarding SBC, we reject the proposition that Bell Atlantic's assets are sufficient to make it reasonably probable that Bell Atlantic would enter GTE's California markets (other than its existing small share of long distance service) in the near future absent the merger. (D.97-03-067, 71 CPUC2d 351, 386.) Although this might demonstrate an ability and capacity to compete, it does not demonstrate an interest in any specific market, or a particular interest in California. Bell Atlantic, like all businesses, has limited resources and has to prioritize its investments. We do not have substantial evidence of a reasonably probability that Bell Atlantic would enter any relevant California market in the near future.

To be clear, we do not hold here that there is no possibility that Bell Atlantic could become an actual potential competitor of GTE California either independently or through combination with another entity under any conceivable set of circumstances. What we do here is apply the standard of a reasonable probability in the near future, not a possibility at some time. The record does not show substantial evidence of a reasonable probability in the near future of such entry.

ORA argues, as does Sprint, that we should err on the side of not eliminating a potential competitor since the risk of making the wrong decision may forever harm competition in California. We have weighed this risk, but we are simply not convinced that we should err on the side of caution and deny the merger in order to retain the possibility that Bell Atlantic might one day become a competitor in California. Rather, there is insufficient evidence to conclude that Bell Atlantic would enter the market absent the merger in any reasonable view of the near future. Moreover, we find that the proposed merger has several pro-competitive elements, and will stimulate competition.

4.3.3.3. Other Potential Entrants

We need not continue our inquiry, since we find that Bell Atlantic would not have entered any relevant concentrated market absent the merger in the near future on its own or by toehold acquisition. Just as we did in the SBC/Telesis merger decision, however, we continue our assessment and consider the other two factors assuming, for the sake of argument, that Bell Atlantic would have entered but for the merger.

Courts have recognized that even if the acquiring firm would have entered independently or in combination with another entity without the merger, the presence of many other firms which are equally ready and willing to enter makes the issue moot. The theory is that elimination of one potential entrant under those circumstances would not be significant. (D.97-03-067, 71 CPUC2d 351, 387, citing *Mercantile Texas Corp.*, 638 F.2d at 1267.)

The evidence here is compelling that there are many other firms that are as ready, willing and able as Bell Atlantic to enter California, including into GTE California's service area. These firms include AT&T, MCI, Sprint and SBC. These firms also include U.S. West, Bell South, ICG, Nextlink, and Electric Lightwave. These latter firms are smaller, are perhaps somewhat less able, and might be characterized as "second-tier" firms. Nonetheless, these second-tier firms are significant potential entrants, and have the ability to grow, if not to merge, and become first-tier firms, as have other firms in this fast changing telecommunications market. Moreover, there are numerous other facilities-based CLECs, cable companies, resale CLECs, and wireless companies that are ready, willing and able to vigorously compete in California.

Many of these competitor firms have unique advantages that Bell Atlantic does not enjoy. For example, AT&T has a world-famous brand name. Astonishingly, a wide margin of Bell Atlantic and GTE customers (by nearly 2 to 1) would prefer to have AT&T provide local and long distance service rather than Bell Atlantic or GTE, even in Bell Atlantic's and GTE's own franchise service territories. AT&T is plainly better able to compete in California's local exchange market than Bell Atlantic. This is generally also true for MCI and Sprint, if not others. Thus, even if Bell Atlantic could somehow be considered an actual potential competitor (which we find is not the case), its merger with GTE would not adversely affect competition.

ORA, AT&T and MCI contend their respective national market analyses show the market is concentrated, and there will be no other potential entrants with comparable advantages. For the reasons explained above, we do not find those analyses compelling.

4.3.3.4. Likelihood of Deconcentration or Other Significant Pro-Competitive Effects

Entry by Bell Atlantic would not carry a substantial likelihood of ultimately producing deconcentration or other pro-competitive effects, given its lack of facilities, virtually no customer base, and little brand-name recognition.

Sprint argues that, if the merger is approved, the loss of Bell Atlantic as a potential competitor would be irreversible. To the contrary, no evidence was presented here convincing us that this merger is irreversible, or that mergers in general are irreversible. In fact, we have approved "spin-offs" of companies in California. When justified, companies can be separated into reasonable parts, and the parts sold for a profit. Mergers are popular today in the telecommunications industry. That has not always been the case in all industries, however, and may not continue to be so in the telecommunications market.

ORA repeats its national market analysis to conclude that the proposed merger will create an HHI index that greatly exceeds the DOJ threshold, thus indicating an extremely concentrated market. For the reasons explained above, we decline to find that ORA's analysis supports a conclusion that Bell Atlantic's entry would produce deconcentration or other significant pro-competitive effects.

We agree with the Attorney General that:

> "If Bell Atlantic entered California telecommunications markets, it would face strong competitors in the markets for intraLATA toll, dedicated access, and some facilities-based basic business services. AT&T, Sprint, MCIWorldCom, SBC and perhaps other major firms have existing plans to enter profitable markets currently served by GTE. There is no basis for concluding that future Bell Atlantic entry would substantially increase the level of competition beyond that provided by these other entrants." (Attorney General Opinion, pages 15-16.)

4.3.3.5. Conclusion

The four criteria are not met to establish that Bell Atlantic would be an actual potential competitor. We now look at other effects of the proposed merger that opponents claim would result in the proposed merger adversely affecting competition: price discrimination, locking up the large business market, non-price discrimination, and a decrease in the amount of benchmarking information.

4.3.4. Price Discrimination

AT&T and MCI argue that the merger will harm competition by enabling applicants to engage in a discriminatory "price squeeze."[63] They allege that applicants can accomplish this by setting "high" access prices (which long distance carriers pay) and "low" retail long distance prices.

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[63] "'A price squeeze occurs when the integrated firm's price at the [upstream] level is too high, or its price at the [downstream] level is too low, for the independent to cover its costs and stay in business.'" (Attorney General's Opinion at page 20, citing *Town of Concord, Mass. v. Boston Edison Co.*, 915 F.2d 17 (1st Cir. 1990).)

According to AT&T and MCI, when a call originates and terminates within GTE's and Bell Atlantic's footprint, applicants will get access at its economic cost at both ends of the call, whereas unaffiliated competitors, like AT&T and MCI, will pay inflated rates for access at both ends of the call. AT&T and MCI contend that applicants thereby gain an artificial and anti-competitive advantage, and that the effectiveness of the price squeeze increases as monopoly ILECs increase the size of their monopoly franchises through mergers. If the merger is approved, AT&T and MCI recommend that intrastate access charges be reduced to cost as a condition of merger approval.

We considered and rejected the same argument in the SBC/Telesis decision. (D.97-03-067, 71 CPUC2d 351, 390.) The price squeeze argument is not merger related, but is a problem IECs have with ILECs being able to offer interLATA services before access charges are reformed. Further, to the extent there is an incentive to engage in a price squeeze, GTE has the same incentive even without the merger because GTE already provides interLATA service.

Merger opponents did not present empirical evidence to support the theory. Not only GTE, but other firms as well, allegedly have had the incentive to engage in some form of price squeeze for years. We are not convinced of the theory absent evidence that it has occurred.

Further, even if this artificial advantage were to exist, the record does not establish that the merger will increase the advantage, or increase it to the degree that it would have an adverse effect on competition. That is, AT&T and MCI did not here quantify the effect, if any, or the extent to which it would increase with the merger.

The price squeeze argument also fails for other reasons. The merged entity will not have a reasonable ability to engage in price squeeze, and, in fact, will have a powerful incentive not to engage in price squeeze. Rather, GTE and Bell

Atlantic are required to charge their long distance affiliates the same price per access minute as they do any other carrier. AT&T, MCI, and other IECs, are sophisticated firms that closely monitor access charges and are willing to report unlawful price discrimination to regulators. Price squeeze (when it is unlawfully different prices to different ILECs) would subject applicants to enforcement and penalties. Thus, to the extent the price squeeze theory relies on different access prices for different carriers, it is not convincing.

Further, even if the same access prices are charged to all ILECs, a price squeeze involves opportunity costs that minimize, if not eliminate, applicants' incentive to implement price squeeze. Most importantly, IECs can bypass—and have the ability to increase bypass of—ILEC facilities, thereby mitigating if not eliminating the ability of the ILEC to engage in price squeeze. That is, price squeeze would drive ILECs to bypass the LEC's facilities altogether, resulting in permanent loss of access revenues.

Moreover, the price squeeze argument is based on the implausible theory that the ILEC can drive the major IECs out of the interLATA business. That is, a firm would engage in price squeeze only it if is more profitable to do so than not to do so. Price squeeze tactics do not finally become profitable until after rivals have been forced from the market. The cost of forcing competitors like AT&T, MCI, Sprint, and others, from the market, however, would be prohibitive. Even if it could be done, reentry would be a near certainty, either by the excluded firm or by a new firm after having purchased the excluded firm's assets at a discount. The most likely result of an attempted price squeeze would be to replace one IEC with another. The merged entity has no conceivable incentive to achieve such a result. The Attorney General agrees. (Attorney General's Opinion, pages 21-2.)

AT&T and MCI reply that the success of a price squeeze does not rely on entirely eliminating IECs, but simply in securing a somewhat larger market share. Again, we are not persuaded absent evidence in support of the theory generally, and specific evidence that this particular merger will increase the advantage (if one exists) to the degree that it would have an adverse effect on competition.

We concur with the Attorney General when he concludes that we do not here have "any probative evidence that the merged entity would have the requisite incentive or ability to engage in a price squeeze against long distance suppliers." (Attorney General Opinion, page 22.) Thus, we do not find the price discrimination argument compelling.

Even if we did, we would reject the recommendation of AT&T and MCI that intrastate access charges be reduced to cost as a condition of merger approval. Access charges—as are all rates—are set to balance many different and often competing objectives and criteria. A merger application is not the proceeding to address the many complex issues that surround access charges. Parties may address access charge reform in appropriate other proceedings.

4.3.5. Large Business Customers

Merger opponents assert that the merger will harm competition by enabling the merged entity to "lock up" the large business market both in-franchise and out-of-franchise. For example, applicants will "leverage" their position, and sell a package of local and competitive services at a price discount across multiple geographic territories to the disadvantage of competitors, according to opponents.

We are not convinced. There is already more competition for large business customers than for any other class of customers. Large business customers are among the most sophisticated of customers in purchasing telecommunications services. They often have professional telecommunications staffs, or are able to purchase telecommunications consulting services, to assist in assessing options. There are too many options, with more being developed each day, for applicants to be able to adversely affect competition for large business customers. Rather, the additional competition that will occur as applicants try to secure large business customers will be healthy.

Moreover, packaging services is desirable when it meets customer demand, and is not anti-competitive when it is cost-justified. This proceeding is not the proper place to review existing cost and price data (even if a national market for packaged services currently existed), or future cost and price data (for a hypothetical future market). Such inquiry should have been, or should be, in a proceeding that establishes costs and prices for packages of services. Alternatively, it may be considered in a complaint proceeding. The speculation that applicants might engage in some future illegal act is not a sufficiently compelling argument to deny or condition the merger. Rather, applicants' rates are set by this and other Commissions to balance all proper concerns, and applicants are subject to sufficient laws to prohibit their setting unregulated rates in an illegal manner.

4.3.6. Non-Price Discrimination

Merger opponents argue that CLECs are harmed by applicants engaging in non-price discrimination (e.g., degrading the quality of inputs used by CLECs, delaying or denying access to UNEs and collocation facilities, delaying the installation of new interconnection trunks, delaying access to OSS, delaying repair of leased facilities). This discrimination has the effect, according to merger opponents, of preventing, or at least delaying and harming, competition. Moreover, the incentive to engage in this behavior is increased by the merger, according to opponents, because applicants will internalize "spillover" effects. That is, effects before the merger caused by one applicant that are external to that applicant, but experienced by the other applicant, will become internalized when experienced by the combined entity once merged.[64] We are not persuaded, however, that non-price discrimination is a factor that justifies conditioning approval of, or denying, the merger.

For example, steps are underway to open local markets. GTE California has entered into 56 interconnection agreements, with others pending approval. Any new entrant can adopt the terms of any effective agreement. There are 249 completed or pending collocation agreements in 80 GTE California central offices, allowing competitors to reach 62% of GTE California's access lines. Pursuant to the Act, applicants have very limited, if any, ability to prevent CLEC entry, even if doing so is to their advantage.

Moreover, GTE has established a web-based Wholesale Internet Service Engine to simplify and expedite service ordering and access to OSS. GTE provides CLECs with information guides, training programs, and help desks, plus staff to visit CLEC sites to help CLECs resolve technical problems. These actions show applicants are taking direct steps to facilitate competition.

Further, GTE is obligated by the Act to provide nondiscriminatory access to UNEs, resold services, and other products and services. Numerous effective interconnection agreements contain procedures for handling disputes

[64] For example, proponents of this theory say that if GTE successfully engages in non-price discrimination to reduce competition from CLECs within GTE's service area, CLECs pursuing a national market will be discouraged and disadvantaged not only with respect to GTE, but the rest of the nation as well. The CLECs will be harmed nationally because a potion of the national market (i.e., within GTE's service area) is unavailable (or less available) to them. This reduces their ability to compete in Bell Atlantic's service area for those customers in Bell Atlantic's service area that seek to include GTE's service area via one telecommunications firm. GTE would be indifferent to the effect on Bell Atlantic pre-merger, but would internalize the effect post-merger. Thus, proponents of the spillover effect argue GTE has an even larger incentive to engage in non-price discrimination post-merger.

between GTE and CLECs. As appropriate, complaints may be filed before federal and state regulators, and in court.[65] In addition, CLECs may bypass GTE California's facilities. Thus, the opening of markets, along with regulatory oversight and facilities bypass severely limit, if not eliminate, the ability of GTE California to discriminate against, or exclude, competitors.

Moreover, it is exceedingly difficult for an ILEC to degrade the quality of service on some lines without simultaneously degrading the quality of service it provides to its own customers. As applicants' witness Teece testifies, it is simply not possible for an ILEC to selectively degrade quality to disadvantage competitors.

Even if non-price discrimination occurs (which we do not conclude it does here), we are not persuaded that it will change as a result of the merger. For example, AT&T and MCI complain that GTE does not now have a pre-qualifying process for DSL-capable loops. If true, that will not change solely as a result of the merger.

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[65] Sprint argues that regulatory oversight and timely enforcement become increasingly more difficult as the market becomes more complex. Sprint says applicants miss the point when applicants say competitors may rely on dispute resolution procedures and regulatory oversight to prevent exclusionary conduct by applicants. Sprint contends that the delay involved in resolving disputes may impair a competitor's ability to compete. We agree there may be delays, and that this may affect competition. We disagree on what this means for this merger application. Telecommunications markets are becoming more complex as they become more competitive. There are advantages and disadvantages from competitive markets, just as there are advantages and disadvantages from monopoly markets. One disadvantage of competitive markets may be the time it takes for regulators, legislators and judges to resolve complex, technical disputes between competitors. On balance, however, we continue to believe competitive markets are superior. We are not convinced by Sprint that any increasing complexity or resulting delays justify conditioning or denying the merger. We will certainly not deny the merger simply because telecommunications markets are becoming more complex, and delays may occur in future dispute resolutions. Rather, we think reliance on dispute resolution procedures, plus regulatory and court oversight, is reasonable.

Merger opponents claim that the incentive to employ non-price discrimination will increase due to the "spillover" effect. That is, the advantages of incumbency increase as an ILEC's territory expands with a merger. We are not convinced. As applicants point out, the "spillover" effect, if it occurs at all, may not be positive. Applicants show, for example, that before a merger an ILEC might over-invest in exclusionary behavior to encourage CLECs to go elsewhere. After the merger, however, such actions may result in CLECs entering the territory of the new merger partner. As a result, the "spillover" effect may be negative, and such behavior may decrease.

Sprint argues that "spillover" effects cannot be negative. Sprint says that applicants' example assumes the competitor in GTE's territory will not be a competitor in Bell Atlantic's territory unless GTE makes it too difficult to compete with GTE. Sprint contends that under applicants' own theory, applicants' competitors must compete as national entrants, and will therefore enter all markets. We disagree. Applicants may seek to become national competitors, but the "spillover" theory does not require two hypothetical merger partners to have that strategy.

Sprint cites several examples to demonstrate alleged non-price discrimination. For example, Sprint argues that GTE California had difficulties processing orders to resell local services, and does not provide adequate OSS. As GTE testified, however, GTE is currently developing a fully automated ordering system with sophisticated OSS. Thus, we think the problem is being addressed.

Moreover, Sprint's experience is not shared by all firms. AT&T testified that it has a strong working relationship with GTE, generally receives exceptional service from GTE, and is concerned that the merger, if anything, will degrade GTE California's ability to meet AT&T's needs.[66]

Even if there is a problem (which we do not conclude there is), it is not clear that it is merger related, or will be made worse by the merger. Sprint offers no solution other than denial of the merger to address its concern. We are not convinced this problem (even in conjunction with other alleged problems) justifies denial of the merger.

Sprint argues that GTE California may have spent millions of dollars attempting to open local markets, but they are not open. Sprint wonders if GTE California really seeks to develop an effective OSS, or simply provide a basis for claiming they were making an effort. Sprint concludes that "the more than three-year delay in development, and the continued failure to provide fully automated interface, begin to appear intentional." (Sprint Reply Brief, page 25.)

We wish all telecommunications markets were fully competitive now. The transition to perfectly competitive markets, however, is complex, and implementing OSS may be complicated. Sprint presents insufficient evidence for us to conclude here that GTE California is intentionally preventing competition, and that the merger should, therefore, be approved with conditions or denied.

Sprint points out that GTE erroneously billed Sprint resale customers directly. GTE has corrected these errors. Sprint responds that the problem is not totally resolved. To the contrary, the problem is solved now by a manual bill pull and review process. A fully automated process is scheduled for full implementation in March 2000.

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[66] Relatedly, AT&T witness Tyler testified that: "It has been my experience that GTE is generally in the top tier of access providers in the area of dedicated and switched access performance." (Exhibit 109, page 9.)

Sprint argues that GTE engages in overly aggressive litigation for the purpose of harming competition. We decline to infer anti-competitive intent from the cited examples of applicants' exercising their rights before the Commission and the courts.

Sprint asserts that it does not oppose legitimate legal advocacy, but points out that such advocacy can have the effect of hindering competition. We agree, but again decline to find any anti-competitive intent, or any justification for denying, or conditioning approval of, the merger.

Sprint contends that GTE has restricted access to xDSL service, requiring that the ADSL connection terminate at an ISP, whereas Sprint's ION needs to terminate at the Sprint network. In fact, GTE points out that its ADSL tariff (filed with the Federal Communications Commission (FCC)) contains no such restriction, and Sprint may connect the ADSL line to an ISP, a content provider, a corporate network or a CLEC network.[67]

Sprint argues that GTE's ADSL service handles data only, whereas Sprint's ION requires lines that can accommodate both data and voice. Even if true, there is nothing that prevents Sprint from purchasing an unbundled loop and collating its own digital subscriber line access multiplexer (DSLAM) equipment.[68] Further, Sprint does not assert, and has not demonstrated, that GTE's offering

[67] Sprint holds a certificate as a California CLEC to provide both resale and facilities-based service. (D.97-08-045.)

[68] Indeed, Sprint says it plans to collocate DSL equipment in ILEC central offices to gain access to UNE loops, and plans to deploy broadband enabling equipment, such as DSLAMs, widely in major markets. Sprint plans deployment in 1,000 ILEC central offices by early 2000, and ultimate deployment in more than 1,600 ILEC central offices. (Sprint Opening Brief, page 33, citing Exhibit 288, page 7.)

violates any tariff, rule, order or law. GTE is not required to provide exactly every configuration of every service any customer may want.

Sprint argues that applicants' actions make substitutes for ILEC inputs not cost-effective. Sprint contends that the issue is not whether an alternative exists, but whether the CLEC and its customer are less well off by use of the alternative.

Sprint is right that cost-effectiveness is fundamental to all customer and business decisions. We decline, however, to make applicants offer every combination of every possible service. Sprint does not propose any specific conditions related to xDSL service, and we have insufficient evidence from Sprint to order any particular condition with merger approval regarding xDSL. Moreover, Sprint fails to make a compelling showing that the merger must be denied or conditioned to meet Sprint's individual needs with respect to ION, or another possible offering.

Remarkably, Sprint contends that the most dramatic advantage of Sprint ION is with on-net to on-net communication. That is, each consumer's benefit from Sprint ION increases with the number of other Sprint customers on ION. A reasonable extrapolation of this claim is that the most benefits occur if Sprint is the monopoly provider, and Sprint ION is the monopoly service. We think this is unlikely to happen. Sprint—just as all carriers in a similar situation—may need to consider creating other ways for ION benefits to grow without monopolizing customers and service. We are not convinced by Sprint that ION service, however desirable it might be, justifies denying or conditioning the merger.

Sprint asserts that applicants' ability to limit Sprint's deployment of ION reduces Sprint's ability to attract subscribers, and will delay or reduce Sprint's ability to earn adequate returns. Ultimately, Sprint says such conduct would discourage Sprint from investing in future service capabilities. Even if true, Sprint does not state that it will not proceed with ION deployment and service. We agree with the Attorney General when he concludes that:

> "...the vast majority of the costs of providing the ION service...would not be jeopardized by any incentives resulting from this merger." (Attorney General's Opinion, page 18.)
>
> "It is, therefore, unlikely, that the merger will affect Sprint's decision to provide ION service..." (Attorney General Opinion, page 18, footnote 102.)

Finally, even if non-price discrimination exists and will increase due to the merger (which we do not find here), merger opponents do not quantify the effect. Without better information, we are unable to find that the costs outweigh the substantial and quantifiable pro-competitive benefits.[69]

4.3.7. Benchmarking

Merger opponents contend that the merger will decrease regulators' ability to benchmark GTE California's performance and actions with those of other utilities. Opponents say this will increase regulatory burden. No party recommends the merger be denied on this basis, but that this effect should be considered.

We consider this effect, but do not find it to be a reason to condition or deny the merger. First, the merger will combine two holding companies. The ILEC affiliates of GTE and Bell Atlantic will remain as separate corporate entities. GTE California will continue to report separately to this Commission, and Bell Atlantic's ILECs will continue to report separately to other commissions.

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[69] Sprint argues that even without specific quantification, it has shown that the effects are material and substantial. We conclude the benefits are material and substantial (e.g., $168.1 million NPV), and outweigh the disadvantages of the merger, if any.

Sprint argues that the ILECs of the merged entity will no longer be independent, and that the resulting data will have less independent value. Even if true, we do not think this is sufficient reason to condition or deny the merger.

Second, as more CLECs enter the market, more (not less) benchmarking information will become available. Third, we retain our authority to direct GTE California, and others under our jurisdiction, to accumulate and report any reasonable data we find necessary. Finally, even if benchmarking data declines slightly, that is simply not a reason to disapprove the merger.

4.4. Balance of Pro-Competitive and Anti-Competitive Effects

Parties also address whether or not the pro-competitive effects of the proposed merger outweigh the anti-competitive effects. This balancing test does not annul the requirements of §§ 854 (b)(3) and (e), in which applicants must prove by a preponderance of the evidence that the proposed merger does not adversely affect competition, and the Commission must make that finding. Nonetheless, we address parties' comments on this balance in further consideration of the proposed merger.

We agree with applicants that the merger will not adversely affect competition. We also agree that the merger will have several pro-competitive effects bringing benefits to California.

AT&T and MCI disagree, stating that applicants have failed to provide the competitive analysis required under § 854(b)(3). AT&T and MCI criticize applicants' showing, but do not explain with any clarity exactly what analysis they think is required. We are satisfied that applicants have met their burden of proof by a preponderance of the evidence.

AT&T and MCI assert that applicants' promises of pro-competitive benefits are empty words. We do not agree, and with regard to the specifics of entering three out-of-franchise markets, we expect applicants to honor their intentions and commitments. Moreover, anti-competitive claims asserted by opponents are largely based on speculation, or not compelling, as explained above.

AT&T and MCI claim that the planned merger is primarily designed to assist applicants lock up "the one local market subject to some competition, the large national business market." (AT&T and MCI Opening Brief, page 29.) The juxtaposition of "local market" with "national business market" again mixes and confuses markets. Moreover, to the extent there is, or will be, a local national business market, the merger will stimulate, not harm, competition.

AT&T and MCI say that the merger will allow applicants to "maintain their stranglehold on the markets where there is almost no competition, including local and access markets for residential and small business service." (AT&T and MCI Opening Brief, page 29.) For the reasons explained above, the merger will not change GTE California's market share in those markets, but the merger will, in fact, stimulate competition.

AT&T and MCI state that internet services, and other competitive services, will be harmed by applicants' leveraging their monopoly assets to bundle competitive and monopoly services in their expanded franchise footprints. For all the reasons stated above, we think this concern is speculative and is not a reason to condition or deny the merger.

Sprint says we should not reject the merger solely because the amount or value of benchmarking information will be reduced, but we should include this factor in balancing the pro-competitive and anti-competitive effects. We have. We conclude this is not a reason to condition or deny the merger.

ORA asserts that the merger will actually delay GTE's ability to offer innovative, integrated services to its California customers, and to become a first tier national provider. This is so, according to ORA, because GTE's ambitions will be held hostage to Bell Atlantic's receipt of Act § 271 approval.

We are not convinced. We agree that both GTE and Bell Atlantic hope to become even more innovative, provide more integrated services, and achieve first tier provider status, whether merged or not. We do not know, however, how soon GTE would or would not achieve one or more of those goals with or without Bell Atlantic. The evidence shows that Bell Atlantic is doing what it can to obtain Act § 271 authority. We have no information allowing us to conclude that GTE could have on its own achieved certain goals before Bell Atlantic receives that authority. To the extent ORA raises a legitimate concern, we have no more than speculation that GTE will be harmed. We decline to condition or deny the merger based on speculation.

4.5. Weight to Give Attorney General's Opinion

AT&T, MCI, and Sprint recommend that we not be guided by the Attorney General's Opinion, and accord the Opinion little, or no, weight. In support, they contend that the Opinion assesses the effects of the proposed merger solely from the point of view of federal antitrust standards. ORA agrees that the Opinion is too narrowly focused on federal antitrust law, and urges that the Commission apply antitrust standards less rigidly.

We are not persuaded that the Attorney General's Opinion is as narrow as merger opponents claim. The Opinion uses a standard of review for competitive effects based on federal guidelines (e.g., guidelines used by the DOJ and the Federal Trade Commission). It is also based on the Attorney General's understanding and application of § 854. The Attorney General specifically concludes that "the acquisition will not adversely affect competition within the meaning of section 854(b)(3)." (Attorney General Opinion, page preceding Outline of Analysis.)

Nonetheless, consistent with merger opponents concerns, we also apply our own experience with, and understanding of, the telecommunications industry. Even so, we reach the same conclusion as the Attorney General.

ORA says that, according to the Attorney General, the merger does not *decrease* competition. Nonetheless, ORA asserts that the proposed merger raises concerns about meeting federal and state goals to *increase* competition. ORA warns that foreclosing opportunities at this time when so little progress has been made creates a risk to consumers. ORA concludes that the lack of pro-competitive effects combined with merger risks underscores the necessity of ensuring that customers receive a fair portion of the merger synergies, and that ORA's proposed mitigation measures be adopted if the merger is approved.

We are not persuaded by ORA that the merger forecloses unique opportunities where, in ORA's opinion, so little progress has been made. Rather, we think the merger will, on balance, be pro-competitive. We agree with ORA it is vital that ratepayers receive a fair portion of merger synergies, and we produce that result with the economic benefits amount determined above. We address ORA's proposed mitigation measures later in this order.

AT&T, MCI and Sprint contend that the Attorney General confuses the law, and misapplies the burden of proof, when he concludes "that these intervenors [AT&T, MCI, Sprint, ORA] have failed to meet the burden required to successfully challenge this merger..." (Attorney General Opinion, page 1.) To the contrary, there is no doubt that the Opinion first assesses the merger on its own merits and concludes that it will not adversely affect competition. Only then does the Attorney General review the arguments of merger opponents, and conclude that they do not disturb his initial finding. AT&T, MCI and Sprint are simply wrong that the Attorney General has confused the law and misapplied the burden of proof.

AT&T, MCI and Sprint reargue their positions on disputed facts and issues where the Attorney General reaches different conclusions. Similarly, they point out what they assert are weaknesses in the Attorney General's opinion. We take these into account in determining the weight to give the Attorney General's Opinion, but nothing in the argument presented by AT&T, MCI and Sprint convince us that the Opinion should be accorded as little weight as AT&T, MCI and Sprint recommend.

Finally, AT&T, MCI and Sprint state that the Opinion is almost useless because it relies extensively on information outside the record, none of which was subject to discovery and cross-examination. AT&T, MCI and Sprint overstate their case. The Opinion contains 147 footnotes within its 26 pages. The clear majority of the Opinion, including the 147 citations, rely on evidence and argument in this case (e.g., exhibits, transcripts, briefs), Commission decisions, the Public Utilities Code, court decisions, and the Act. We may rely on all of these in reaching our decision.

AT&T, MCI, and Sprint contend that consideration of the Attorney General's Opinion deprives them of due process. We are not convinced. The schedule (including the date for the Attorney General's Opinion) was adopted only after comment from the parties on how the Opinion would be incorporated in this proceeding. (PHC-1 Tr. 63.) AT&T, MCI and Sprint were aware of the process, and should have raised due process concerns at the PHC. They did not. The adopted approach was the same as that used in the SBC/Telesis merger. It is untimely for them to raise this concern only after the Attorney General's Opinion was filed.

More importantly, however, parties addressed the Attorney General's Opinion in their reply briefs. ORA, AT&T, MCI, and Sprint did so, and we consider their comments in determining the appropriate weight to give the Opinion. We thank the Attorney General for a well-written, well-reasoned, and well-documented Opinion.

5. PUBLIC INTEREST CRITERIA

Before authorizing a merger, § 854(c) requires that we consider several public interest criteria. In doing so, we need not find that each criterion is independently satisfied, but we must "find, on balance, that the merger...is in the public interest." (§ 854(c).)

Applicants assert that the proposed merger satisfies each criterion, and is, therefore, in the public interest. Public Advocates, Greenlining, and LIF agree, as long as the CCA is adopted as proposed.

ORA claims that the proposed merger is not in the public interest absent adoption of ORA's recommended mitigation measures. AT&T and MCI argue that applicants have failed to prove the proposed merger is in the public interest.

Sprint states that applicants have not yet made many important decisions. As such, Sprint concludes that there is no substantial evidence upon which the Commission may find that the merger will meet several of the required criteria. Moreover, Sprint believes the anti-competitive effects of the proposed merger outweigh any benefits and preclude our finding that the proposed merger is in the public interest.

It is useful here to repeat a few undisputed facts stated by applicants that are helpful in our consideration of the public interest criteria. The merger is between two holding companies that do not have any material overlapping operations in California. The transaction does not involve an operational consolidation of the operating subsidiaries. No changes are planned in the senior management of GTE's California utility subsidiaries. From the customer and Commission perspective, the entities that provide services to California customers today will be the same entities providing services after consummation of the merger.

5.1. Financial Condition

First, we must consider whether the proposed merger will "maintain or improve the financial condition of the resulting public utility doing business in the state." (§ 854(c)(1).)

GTE and Bell Atlantic are both financially sound companies. No party contends otherwise. The merger will give the combined company even more financial resources and flexibility. Based on 1997 financial statements, the merged company will have combined assets of $96 billion, total annual operating revenues of $53 billion, and annual net income of $6.9 billion.

Sprint argues that applicants have not determined what corporate structure(s) will be used to compete in California, and, consequently, the Commission has no evidence upon which to find the merger will maintain or improve the financial condition of the resulting public utility. We disagree.

GTE will become a wholly owned subsidiary of Bell Atlantic, and GTE's California utility subsidiaries will become second-level subsidiaries of Bell Atlantic. Applicants say the same entities that provide services to California customers today will provide services to California customers after consummation of the merger. Any changes will be made only after obtaining approvals to the extent required by the Public Utilities Code and this Commission. The corporate structure is reasonably well known.

AT&T and MCI point to evidence and testimony wherein applicants state they have not decided what corporate structure(s) or brand will be used to compete in California. AT&T and MCI claim applicants are thereby hiding the ball on issues that relate to possible harms. We are not convinced.

Applicants forthrightly respond in the evidence and testimony to which AT&T and MCI refer that many decisions have not yet been made. This does not conflict with the testimony that the California utility subsidiaries will remain the same, unless and until changed based on receipt of necessary approvals. Applicants are simply being candid that changes are being considered, but no decisions have been made.

AT&T and MCI state they are concerned that "[i]f applicants are planning on tampering with GTEC's structure and assets, that fact is important to the Commission and its on-going oversight of GTEC's operations here." (Opening Brief, page 41.) We are not concerned. GTE California might "tamper" with its assets even without the merger. Whether done with or without the merger, however, GTE California must comply with applicable Public Utilities Code and Commission requirements. Nothing about the merger negates applicants' responsibilities in this regard.

Thus, the corporate structure is sufficiently known to reach a judgment, based on a preponderance of the evidence, whether or not the proposed merger will maintain or improve the financial condition of the resulting public utilities doing business in the state. We determine that it will not only maintain, but will improve, the financial condition of GTE's California utility subsidiaries.

5.2. Quality of Service

Next, we must consider whether the proposed merger will "maintain or improve the quality of service to public utility ratepayers in the state." (§ 854(c)(2).)

5.2.1. Positions

Applicants state that there is no reason to believe that the quality of service experienced by GTE's California customers will deteriorate since the merger is taking place at the level of the parent holding companies. In fact, according to applicants, the proposed merger will allow GTE to adopt Bell Atlantic's service quality best practices, thereby improving the level of service quality enjoyed by GTE's California ratepayers.

Public Advocates, Greenlining, and LIF agree since, they assert, the CCA will improve the quality of service to California's low-income, minority, limited-English speaking and disability communities. ORA accepts applicants' assurances that service quality will be maintained or improved because applicants have agreed to provide ORA with specific service quality reports.

AT&T and MCI contend that the proposed merger will decrease service quality due to its harmful effect on competition. Moreover, AT&T and MCI say applicants have not substantiated their bare assertions regarding adoption of best practices. Sprint says applicants have made no decisions about how services will be changed and there is, therefore, no substantial evidence upon which to find that the merger will maintain or improve service quality.

NorthPoint Communications, Inc. (NorthPoint) says applicants have failed to show they will maintain or improve service quality to wholesale xDSL customers. To mitigate possible service degradation, NorthPoint recommends three conditions with merger approval.

5.2.2. Discussion

We agree with applicants. There is simply no reason to believe that the quality of service experienced by GTE's California customers will deteriorate given that the merger is taking place at the level of the parent holding companies. Moreover, increasing competitive pressures will make providing quality service a business imperative.

The importance of service quality to the ultimate success of applicants' business is further reflected in the fact that each company ties executive compensation directly to indices of service quality. There is no indication that the merged entity will change that practice.

Further, applicants are committed to adopting each other's best practices. This promises to at least maintain, if not improve, service quality.

AT&T and MCI state that applicants have hidden the ball from parties and the Commission regarding best practices. According to AT&T and MCI, applicants continually hide behind the assertion that no decisions in these areas have been made, rather than identify any specific new service, product, or best practice. AT&T and MCI claim that applicants' inability to identify a single service improvement more than a year after they announced their proposed merger is astonishing, and is an enormous hole in their case.

Applicants claim that the inability to announce final decisions regarding several corporate governance and operations issues, including best practices, is an unavoidable consequence of there being no joint management in place, with no joint management able to make such decisions until the merger is consummated. We generally agree with applicants. The strongest showing would contain specific probable best practices that are likely to be adopted. The absence of such showing, however, does not mean applicants fail to meet their burden of proof. Applicants present examples of work completed by Merger Integration Teams to illustrate the process that will lead to the adoption of best practices. It is clear that applicants are working to identify best practices that will improve customer satisfaction.

AT&T and MCI state that without identifying the specific best practices, applicants essentially ask the Commission to assume applicants will take steps to adopt practices necessary to make them a better company. AT&T and MCI say the public interest finding cannot be made on the basis of promises and speculation, when the company will not even identify what practices they intend to follow. We disagree.

Applicants do not ask that we simply assume they will adopt best practices. Rather, applicants must achieve several things, including best practices, to fund the $84.1 million (NPV) ratepayer share of merger benefits. Applicants have given examples of the areas in which they will seek to implement best practices. Even without stating the precise specifics, the examples plus the dollar commitment provide a preponderance of the evidence that service quality will be maintained, if not improved.

Moreover, applicants have committed to maintaining or improving service quality as part of the CCA. We are confident that the more than 450 community organizations and individuals who signed the CCA, along with the

CCC, will monitor whether applicants are honoring this commitment. We also believe that improving service quality to one population generally improves service quality to all customers. That is, service quality improvements to the otherwise under-served communities will generally involve equipment or processes that will improve service quality to all customers, just as adding more customers improves the benefits of the network to all customers. Thus, the CCA provides additional evidence that service quality will be maintained, if not improved.[70]

Further, applicants agree to ORA's recommended additional service quality reporting requirements. (See Attachment D.) We adopt ORA's recommendation, and agree with applicants that this further demonstrates applicants' commitment to providing service quality.

Sprint, AT&T and MCI raise service quality concerns regarding wholesale service. We agree with applicants that the merger will not adversely affect the quality of service provided to GTE California's wholesale customers. For example, we do not agree with Sprint that the merger will increase GTE's ability and incentive to engage in anti-competitive conduct with respect to CLECs who are also GTE's wholesale customers, for the reasons explained above in the chapter regarding competition.

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[70] AT&T asserts in comments on the PD that signatories of the CCA will not monitor applicants' service quality. To the contrary, testimony addressed remedies that such signatories might pursue if applicants fail to honor the CCA, including applicants' commitments to improve service quality. AT&T contends signatories to the CCA will have no interest in monitoring applicants' wholesale service quality, and have no knowledge upon which to do so. Even if true, we are confident that AT&T and other wholesale customers are in a position to monitor applicants' wholesale service quality, and will pursue remedies before us and others if and when necessary. Moreover, even if signatories to the CCA do not monitor wholesale service quality, this neither diminishes nor negates the role of the CCA in maintaining, if not improving, retail service quality.

AT&T and MCI raise concerns regarding OSS. AT&T, for example, contends that the proposed merger threatens to disrupt critical on-going negotiations between AT&T and GTE, and separate critical negotiations between AT&T and Bell Atlantic, relating to OSS. According to AT&T and MCI, when asked about the effects of the merger on GTE's account teams assigned to CLECs, such as AT&T and MCI, applicants could only say those decisions have not been made. At the same time, AT&T and MCI say that dollar savings from terminations and relocations associated with combing CLEC wholesale account teams by the merged entity will result in harming and delaying on-going and intense negotiations between CLECs and applicants over implementation of OSS.

We are not convinced. The proposed merger may or may not disrupt on-going negotiations relating to OSS. It is just as likely that the merger will produce efficiencies that will facilitate these negotiations. Further, relocations might improve access to account teams, and terminations might eliminate duplications, resulting in increased efficiency. AT&T and MCI present no compelling evidence to the contrary.

AT&T and MCI argue that the significant differences in OSS between GTE and Bell Atlantic require separate negotiations, and that this will not change as a result of the merger. Rather, AT&T and MCI say that the merged entity's reduced expenses for account teams will mean worse customer service, and, therefore, reduced service quality.

Merger opponents speculate about any number of possible bad outcomes. We are convinced by applicants, however, that opponents' concerns are misplaced. Applicants testified that savings opportunities will not be pursued if it means that CLECs are not provided the necessary service. Applicants have committed to a Change Management Process, and CLECs will have the opportunity to be involved in any changes applicants make.[71] Applicants will be subject to the Commission's OSS requirements and performance measures. The OSS performance measures will test, among other things, whether applicants' service quality to wholesale customers is maintained.

Further, applicants testified that they expect very minimal severance in the wholesale area, with most severance in G&A, product marketing and procurement. Applicants testify that they will honor interconnection agreements. We have every reason to believe that they will, and expect to see complaints if they do not. Moreover, it is unclear that any concern over changes in account teams is related to the merger, since account teams may change over time with or without the merger.

AT&T and MCI say that applicants are grappling with how to integrate their vastly different systems, and that this threatens to undo much of the work AT&T and MCI have accomplished to obtain operational OSS from each applicant. Applicants, however, do not expect any operational consolidation from the merger. We think, at worst, this means things will stay the same. As opportunities develop for integration and efficiency through best practices, we believe OSS will improve.

AT&T and MCI conclude that the system integration process will ultimately hinder CLECs ability to compete against GTE California when CLECs are unable to access customer information or exchange data. We think this concern is overstated. We are confident that OSS matters will be resolved whether the merger application is granted or denied.

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[71] Applicants' Change Management Process involves notifying CLECs of changes to applicants' systems, and providing CLECs an opportunity to comment on the proposed change. This process seeks to minimize disruptions. (Exhibit 13, page 17, lines 13-17.)

Sprint asserts that applicants admit they have not yet made many decisions on how services will be changed. Sprint concludes that there is, therefore, an absence of substantial evidence upon which to find the merger will maintain or improve the quality of service. We think the evidence cited above (e.g., merger at parent level, executive compensation tied to service quality, commitment to adopt each other's best practices, commitment to fund benefits to ratepayers, commitments in CCA, additional service quality reporting, OSS development, commitment to Change Management Process, minimal severance in wholesale area, no operational consolidation from the merger), even if without specific decisions on service changes, demonstrates it is more likely than not that service quality will be maintained, if not improved, as a result of the proposed merger.

NorthPoint states that loop information at the pre-order stage is critical for the efficient provisioning of competitive DSL service. NorthPoint recommends three conditions on merger approval to address this concern: that applicants (1) adopt Bell Atlantic's process for inventorying central offices and compiling an electronically accessible loop pre-qualification data base for all customers (i.e., competing CLECs and applicants' affiliates alike), (2) make such information available via a mechanized pre-ordering interface system, and (3) develop a mechanized flow-through ordering process for xDSL capable loops.

We agree with NorthPoint that loop information may be important to efficient provisioning of DSL service. To the extent CLECs need this information, however, it is needed from GTE with or without the merger. As such, GTE should, with or without the merger, provide this information to the extent reasonable so that CLECs may serve customers, and do so without needless delay. If GTE fails in this, CLECs may seek relief through other proceedings as necessary and appropriate.

We decline, however, to adopt these requirements as conditions of merger approval. The need for loop information is independent of the merger, and we will not condition approval of the merger on matters unrelated to the merger.

5.3. Quality of Management

We must also consider whether the proposed merger will "maintain or improve the quality of management of the resulting public utility doing business in the state." (§ 854(c)(3).)

Applicants state that current management of both GTE and Bell Atlantic are qualified to manage California utility operations, and the combined management will be as well. No party asserts otherwise. We agree with applicants. Moreover, the merger is taking place at the parent company level. We accept applicants' statement that there will be no immediate impact on the management of GTE's California utilities, and that no changes in GTE's senior management are currently planned. Thus, the proposed merger will at least maintain the quality of management. To the extent the proposed merger will give GTE access to Bell Atlantic's management best practices, if any, the proposed merger may actually improve the quality of GTE's management.

ORA, Sprint, AT&T and MCI contend that applicants have not provided sufficient evidence for us to make a finding that the proposed merger will maintain or improve the quality of management. For example, Sprint asserts that applicants have not identified specific management practices that will be adopted or, once adopted, when they will be implemented. AT&T and MCI contend that the proposed merger has the potential to reduce the quality of management of the remaining California utilities by moving management out of state, or replacing GTE account team representatives with personnel from Bell Atlantic.

These concerns provide us no reason to conclude that the merged company will compromise the management of GTE's California utility subsidiaries. Specific management practices need not be specified, nor when they will be implemented, to determine that the proposed merger will maintain the quality of management. Rather, both GTE and Bell Atlantic management have demonstrated they are capable of successfully running a utility, and nothing about the merger will change that.

Further, it is only speculation that GTE management might be moved out of California and, even if they are, whether that will reduce the quality of management. Moreover, we previously herein rejected the concern of AT&T and MCI regarding account team representatives.

On the other hand, we have the testimony of applicants' witnesses that management expects to be stable barring failures to perform. We also have testimony that management will be shared equally through the presence of co-Chief Executive Officers along with the appointment of an equal number of former GTE and Bell Atlantic Board members to the new Board of Directors. Applicants have, by a preponderance of the evidence, demonstrated that the proposed merger will maintain or improve the quality of management of the resulting public utilities doing business in the state.

5.4. Affected Public Utility Employees

We must consider whether the proposed merger will "[b]e fair and reasonable to affected public utility employees, including both union and nonunion employees." (§ 854(c)(4).)

We agree with applicants that the proposed merger will be fair and reasonable to affected public utility employees, including both union and non-union employees. The merger does not involve an operational consolidation. Thus, no material impact on California staffing levels or hourly labor is expected. Elimination of duplicative administrative functions will likely occur at the headquarters level. On the other hand, the various growth opportunities created by the merger will most likely result in new opportunities for GTE employees.

In addition, GTE has made commitments to its employees to ensure that the merger is fair and reasonable. For example, GTE has committed to maintain the level of pension benefits for five years following shareholder approval of the merger. GTE has also committed to maintaining the GTE Savings Plan 401(k) and current severance programs for at least one year following shareholder approval.

The merger by itself will not affect union contracts, and the collective bargaining process will continue to be utilized. The Communications Workers of America and the California Labor Federation, AFL-CIO have each expressed their support for the merger. No employee or employee group testified to any concern that the merger would be unfair or unreasonable to either union or nonunion employees.

Sprint contends that applicants have made no decisions with respect to the number of employees of the merged entity and there is, therefore, a lack of substantial evidence upon which the Commission may find the merger will be fair and reasonable to affected public utility employees. We disagree. It would be premature for applicants to make a specific decision now, before the merger is approved, about the number of employees. Further, it would be arbitrary to make such a decision until the Merger Integration Teams have had the opportunity to complete their work.

For all the reasons cited above—including not only the lack of opposition by employees generally, but the specific support of union employees—we find that applicants have, by a preponderance of the evidence, demonstrated that the proposed merger will be fair and reasonable to affected public utility employees, including both union and nonunion employees.

5.5. Affected Public Utility Shareholders

We must consider whether the proposed merger will "[b]e fair and reasonable to the majority of all affected public utility shareholders." (§ 854(c)(5).)

We agree with applicants that the proposed merger will be fair and reasonable to the majority of all affected public utility shareholders. GTE's Board of Directors has concluded that the merger is fair to, and in the best interest of, GTE's shareholders. GTE's financial advisors have each expressed their opinion that the merger is fair to the holders of GTE common stock. Most importantly, the shareholders of both companies have overwhelmingly approved the merger.

No party has suggested that the merger is not fair and reasonable to the majority of affected shareholders. We conclude that, by a preponderance of the evidence, applicants have demonstrated that the proposed merger will be fair and reasonable to the majority of all affected public utility shareholders.

5.6. Effects on State and Local Economies, and the Communities Served by the Merged Company

We must consider whether the proposed merger will "[b]e beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility." (§ 854(c)(6).)

The merger will provide cost savings that will reduce rates through a surcredit. Approval of the CCA means funding of community-based programs to provide telecommunications education and other services to California's traditionally under-served communities. Moreover, we agree with applicants that the merger will generally allow the merged company to become a more effective competitor in various telecommunications markets in California. Among other benefits, this will bring new choices to ratepayers in Pacific's operating territories. The merger will stimulate competition, and create increased prospects for growth, increased employment opportunities, and the potential for increased tax revenues.

These effects are all beneficial to state and local economies, and the communities served by the merged company.

ORA argues that applicants have failed to present sufficient evidence for us to make the necessary finding here. For the reasons stated above, we disagree. Rather, by a preponderance of the evidence, applicants have demonstrated that the proposed merger will be beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility.

5.7. Jurisdiction of the Commission, and the Commission's Capacity to Regulate and Audit

We must consider whether the proposed merger will "[p]reserve the jurisdiction of the commission and the capacity of the commission to effectively regulate and audit public utility operations in the state." (§ 854(c)(7).)

We agree with applicants that our ability to regulate their California public utilities will not be compromised. The proposed merger is at the parent holding company level, and it will not affect the structure or operation of GTE's California utility subsidiaries. All such utilities will continue to provide services in California pursuant to the rates, terms and conditions that we have previously required, and will require in the future. All such utilities will continue to maintain such books and records as we require for effective oversight.

GTE's California utility subsidiaries will continue to be subject to the Public Utilities Code, Commission decisions, Commission General Orders, as well as Commission rules, policies, and practices, regardless of the parent company, or where the parent company is located. Just as we pointed out in our approval of the SBC/Telesis merger, however, we point out here that we will, of course, expect full compliance with prevailing laws, decisions, general orders, rules, policies and practices of this state and this Commission if the merger is consummated. For example, if accounting methods, or ratemaking treatment, differ between GTE and

Bell Atlantic or any affiliate, the merged company shall follow those guidelines and rules that we establish for its California utility operations.

Applicants have also committed to provide additional service quality reports recommended by ORA that are not required by any existing Commission rule or order. We agree with ORA that these additional monitoring reports will facilitate our ability to regulate and audit service quality levels of the merged company's California operations. We expect ORA to monitor these reports, work with applicants to resolve problems and concerns as they arise, and request a Commission proceeding to address concerns that cannot be resolved, if appropriate.

Merger opponents suggest that the location of the merged company's headquarters and operations, if out-of-state, might reduce service and perhaps diminish the ability of the Commission to regulate the merged company's operations. We disagree. Existing GTE headquarters are out-of-state and we do not believe our ability to regulate (including the maintenance of service quality regulation), is affected by the location of GTE's headquarters, or the location of management. Moreover, applicants have addressed some intervenors' concerns through the CCA (which establishes a regular avenue of communications between community-based organizations and the senior management of GTE California), and committed to new service quality reports recommended by ORA.

ORA states that applicants have provided insufficient evidence for us to make a finding that the proposed merger will preserve the Commission's ability to effectively regulate and audit with respect to affiliate transactions and the potential for cross-subsidization. We are not convinced. NRF and other existing regulatory mechanisms (e.g., reporting) contain sufficient safeguards to address cross-subsidization, and nothing about the merger changes NRF and other regulation of GTE's California utility subsidiaries. To the extent the potential exists for cross-subsidization, we agree with the Attorney General that this merger "will not by itself increase the potential for cross-subsidization between California telecommunications markets," and the types of cross-subsidization alleged by merger opponents "would not in any way be exacerbated by this merger." (Attorney General Opinion, page 23.)

AT&T and MCI contend that applicants have not revealed what assets will be used for competition in California. According to AT&T and MCI, parties cannot be assured that applicants will comply with all legal and regulatory requirements, including safeguards designed to detect and prevent cross-subsidies.

We do not conclude that this means applicants fail this or other tests for adoption of the merger. Nothing about the merger excuses applicants from complying with all legal and regulatory requirements. We would not deny the merger because applicants might do something unlawful. Moreover, it would be meaningless to condition the merger on applicants doing nothing unlawful. They must already avoid unlawful conduct.

Further, as stated above, sufficient safeguards exist to address cross-subsidization, and nothing about this merger increases the potential for cross-subsidization. Even if we were to consider such conditions, merger opponents do not propose any sufficiently concrete and compelling additional safeguards that we might adopt. We decline to fashion our own, and we decline to deny the merger based on a concern that existing safeguards might not adequately detect and prevent cross-subsidies.

AT&T and MCI point out we must be vigilant in our regulation because applicants have refused to identify the entities the merged entity will use to provide telecommunications services in California. To the contrary, the 11 GTE subsidiaries identified in Chapter 2 above will continue to be second-level subsidiaries of the new merged company. Changes will only occur subject to receipt of subsequent necessary authorizations.

Sprint states that by reducing the number of independent ILECs, the proposed merger will reduce the availability of independent benchmark reference data, and thereby increase our regulatory burden. For the reasons explained above, we are not convinced.

Just as we did with the SBC/Telesis merger approval, we note for the benefit of clarity that our approval is of applicants' request, and we do not grant any other forms of approval. That is, applicants seek to transfer control of GTE's California utility subsidiaries to Bell Atlantic, which will occur indirectly as a result of GTE's merger with Bell Atlantic. The transaction does not involve an operational consolidation of any local telephone operations or operating companies. GTE's California utility subsidiaries will continue to provide services under the same terms, conditions and regulations that apply before the merger (except for the rate reduction pursuant to § 854(b)(2).) No operations, lines, plant, franchises, or permits of regulated subsidiaries will be merged with the lines, plant, franchises, or permits of any other regulated public utility, except subject to applicants subsequently obtaining the necessary approvals required by the Public Utilities Code and this Commission. It is this request we approve. We do not, for example, approve any other structural or operational changes to any of GTE's California utility subsidiaries.

ORA concludes that applicants have failed to provide sufficient evidence for us to make the necessary finding here, except in the area of increased service quality monitoring reports. We disagree. Rather, by a preponderance of the evidence, we find that applicants have demonstrated that the proposed merger, consistent with our clarification above, will preserve the jurisdiction and capacity of the Commission to effectively regulate and audit public utility operations in the state.

5.8. Mitigation Measures

Lastly, we must "[p]rovide mitigation measures to prevent significant adverse consequences which may result." (§ 854(c)(8).)

Applicants believe the proposed merger satisfies each public interest criterion, no significant adverse consequences will result, and no mitigation measures are warranted. We generally agree, except as explained below.

ORA recommends that the proposed merger be denied but, if approved, proposes three mitigation measures. First, ORA urges an allocation of benefits to ratepayers of no less than $80.5 million per year for 8 years, with the full amount distributed by a surcredit. For the reasons explained above, we find benefits allocable to ratepayers are less than those recommended by ORA, and distribute them by both a surcredit and funding of the CCA. Second, ORA urges that the CCA be funded by applicants, not ratepayers. For the reasons explained above, we decline to adopt this recommendation. Third, ORA urges that specific service quality monitoring reports be ordered. Applicants agree, and we adopt this proposal.

If we approve the proposed merger, TURN recommends three mitigation measures. First, TURN proposes that significant adjustments be made to applicants' forecast of economic benefits. We adopt TURN's recommendation to include revenue synergies, and we increase the period of the long-term (although not to either of TURN's specific recommendations), but decline to adopt other adjustments. Second, TURN contends that shareholders should fund the CCA. For the reasons explained above, we decline to adopt this recommendation. Third, TURN argues that residential basic exchange service should be included in the surcredit billing base. We adopt TURN's recommendation.

AT&T and MCI recommend that the proposed merger be denied but, if approved, recommend six mitigation measures. We decline to adopt these measures.

First, AT&T and MCI propose that the Commission require GTE California to abide by the plain terms of its interconnection agreements with CLECs, particularly with respect to providing combinations of UNEs to those parties that have such term in their interconnection agreements. We decline to adopt this condition. It would be a meaningless act to order GTE California to comply with the terms of its interconnection agreements. GTE California must already do so. If a party to any such agreement thinks otherwise, that party should employ the dispute resolution procedures in the agreement.

Second, AT&T and MCI propose that applicants be prohibited from offering services that are tied to the purchase of a service offered by applicants in their franchise area. According to AT&T and MCI, this condition would help prevent applicants from leveraging their market power. For the reasons explained above, we reject this condition. That is, applicants will not gain market power from this merger. Also, as the Attorney General points out, applicants are public utilities and, as such, they cannot refuse to sell regulated services offered within their franchise areas. To the extent they are able to tie purchases, it is not unreasonable when it meets customer demand, and is not prohibited when cost-justified. This is not the place to determine what are, and are not, the proper costs, and we will not adopt the global prohibition recommended by AT&T and MCI. In fact, a global prohibition would itself be per se anti-competitive. Moreover, since competitors are not prohibited from offering such packages, it would be anti-competitive to prohibit applicants from doing so. This is not to say that it would be unreasonable to apply such condition when justified in a specific instance of improper bundling or tying. Even if such condition is justified in some instance, however, the proposal here is too broad and general to adopt.

Third, AT&T and MCI propose that applicants be prohibited from using their CLEC affiliates to link competitive services with incumbent services in their franchise areas. AT&T and MCI claim using CLEC affiliates would otherwise be a way to circumvent a requirement against bundling or tying services. For the reasons explained above, we reject this condition.

Fourth, AT&T and MCI propose that the Commission reduce intrastate access charges to cost. As explained above regarding price squeeze, this is not the proceeding to address access charge reform. We decline to adopt this condition.

Fifth, AT&T and MCI propose that the Commission adopt a "most favored nation" obligation. That is, AT&T and MCI ask that applicants be required to automatically extend to California entrants the most favorable terms in an interconnection agreement offered in any other state where the combined Bell Atlantic/GTE have operations, either as an incumbent or as a market entrant. We decline to do so. The Act requires that:

> "AVAILIBILITY TO OTHER TELECOMMUNCIATIONS CARRIERS.--A local exchange carrier shall make available any interconnection, service, or network element provided under an agreement approved under this section to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement." (§ 252(i).)

While it might be argued that there is nothing in this language that restricts the availability of an interconnection agreement to only those within the state in which the telecommunications carrier seeks to serve, we draw no conclusion here because parties presented inadequate evidence and argument for us to reach a conclusion. Further, whatever the interpretation, we are not convinced by AT&T and MCI to extend the requirements of the Act to situations where applicants are not incumbents. Moreover, independent of the Act, AT&T and MCI present inadequate justification for this condition as a mitigation measure.

Sixth, AT&T and MCI propose that applicants be made to comply with the competitive checklist in § 271 of the Act. For the reasons explained above, we decline to condition merger approval on applicants complying with the checklist in Act § 271.

NorthPoint recommends adoption of three conditions regarding digital subscriber line service. For the reasons explained previously, we decline to adopt NorthPoint's recommendation.

The Attorney General states that mitigation measures are not required, but that the Commission should share state-level accounting cost information with regulatory agencies in Bell Atlantic states that are closely "affiliated" with California. We agree. We now share public data with any other regulatory agency at their request, and will continue to do so.

5.9. Whether on Balance the Proposed Merger is in the Public Interest

We adopt conditions on, and clarifications of, our merger approval relating to the total amount of benefits allocated to ratepayers, distribution of those benefits by both a surcredit and funding of the CCA, approval of CCA funding, applicants' preparation of service quality monitoring reports, and sharing of state-level accounting cost information. We conclude that the proposed merger, with the adopted conditions and clarifications, is, on balance, in the public interest.

6. REASONABLE OPTIONS TO PROPOSED MERGER

The Public Utilities Codes also requires that:

> "When reviewing a merger...the commission shall consider reasonable options to the proposal recommended by other parties, including no merger...to determine whether comparable short-term and long-term economic savings can be achieved through

> other means while avoiding the possible adverse consequences of the proposal." (§ 854(d).)

Applicants assert that there are no reasonable options. ORA, AT&T, MCI and Sprint state that applicants have not met their burden of proof, and recommend that the merger be denied. ORA, AT&T and MCI say if the proposed merger is approved, it must be approved with conditions (discussed above).

We conclude that applicants have met their burden of proof, and the proposed merger should not be denied. The proposed merger provides short-term and long-term economic benefits to ratepayers, and we establish an equitable allocation of those benefits with ratepayers receiving no less than 50%. The proposed merger does not adversely affect competition. We consider all recommended conditions, and adopt limited conditions for the reasons explained above. The proposed merger, with the adopted conditions, is in the public interest. Therefore, the proposed merger merits approval.

Sprint argues that "no merger may be preferrable [sic] to the proposed merger." (Sprint Opening Brief, page 70.) Importantly, Sprint does not say that the no merger alternative is preferable, only that it may be preferable. We are not convinced.

Sprint neither presents specific data, nor a quantification of benefits, to demonstrate that the no merger alternative produces saving comparable to those from the proposed merger.[72] Moreover, we are not convinced by Sprint that the

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[72] Sprint argues that applicants have failed to present the benefits and savings that arise absent the merger. We find, however, that applicants have met the requirements of § 854, and met their burden of proof. Even if benefits might be overstated (e.g., because applicants do not adjust for early 1999 workforce reductions), they are not zero (i.e., we above rejected assertions of AT&T, MCI and Sprint that benefits might be zero; rather, there are benefits from, for example, elimination of redundant functions, economies of scale, adoption of best practices and revenue synergies that result only from the merger).

Footnote continued on next page

merger creates adverse consequences (see Chapters above on competition and public interest criteria). As such, adoption of a no merger alternative is unnecessary to avoid adverse consequences.

Sprint cites many GTE documents showing that GTE had developed, and was implementing, a go-it-alone strategy for national market entry. Sprint believes GTE would be successful with that strategy. While Sprint might believe this, GTE decided otherwise. We are not convinced that we should take the judgment of Sprint over that of GTE. GTE undertook Project Orion, for example, as a candid evaluation of its strengths and weaknesses. Project Orion concluded that GTE on its own was not up to the task of realizing its aspirations.

According to Sprint, GTE was strategically aligning with, and acquiring, other companies, and considering other acquisitions and possible mergers. Sprint asserts that GTE's strategic needs may have been better served by merging with a company other than Bell Atlantic. Sprint claims that GTE itself concluded that a merger with an RBOC was not the preferred course for addressing GTE's weaknesses.

To the contrary, as applicants point out, Project Orion assumed that Bell Atlantic was not available as a merger partner, as noted on the face of the documents cited by Sprint. Whether or not a merger with other RBOCs (e.g., Bell South, U.S. West) which were considered and rejected would adequately address GTE's strategic needs says nothing about whether GTE believed that a merger with Bell Atlantic—which was not considered at that time—would meet those needs.

Moreover, applicants are not obligated under § 854(b) and (c) to present a specific no merger analysis. Sprint, on the other hand, does not quantify the savings from the no merger alternative. As such, even if the no merger alternative has merit (which we do not find here), we have no quantified estimate to show that the no merger alternative produces savings comparable to the proposed merger.

Sprint contends that the merger announcement was a shock, given GTE's public announcements and efforts to go-it-alone. Even if true, we are not convinced that this justifies further conditioning or denial of the proposed merger. Rather, whether observers were or were not shocked is irrelevant. Even if management was following one course, management has the right to change its views when justified, particularly in the changing telecommunications industry. Whether management "telegraphed" its views in advance is not relevant to our decision.

Sprint also asserts that the decision to merge was not based on a strategic analysis. Whether or not Sprint believes applicants performed an adequate strategic analysis is irrelevant. Whatever the analysis, it was sufficient to convince those within GTE who had authority to make the decision to decide, and for shareholders to vote in favor of the merger. Moreover, the evidence shows that GTE was considering many options. It is likely that GTE's management fully understood the costs and benefits of several alternatives without as concrete an analysis as Sprint argues they should have required. Finally, whatever the analysis used by GTE to reach its decision, the showing before us meets applicants' burden of proof.

Sprint argues that GTE might have been better served by merging with a different company or pursuing its goals on its own. Virtually anything is possible. This assertion does not convince us that the proposed merger should be denied.

7. ELIGIBILITY TO FILE REQUEST FOR INTERVENOR COMPENSATION

In consultation with the Assigned Commissioner, the Presiding Officer filed preliminary rulings regarding intervenor compensation on April 1, 1999, and August 31, 1999. Those rulings find that, pursuant to §§ 1801 to 1812, TURN, Greenlining, LIF, and Public Advocates are eligible to file a claim for compensation. The first ruling also notes that Greenlining and LIF must include their showing of significant financial hardship with their compensation claim. Further, the rulings state that the estimated budgets for Greenlining, LIF and Public Advocates may be excessive, and that Greenlining, LIF and Public Advocates must fully justify their compensation claim, just as must every intervenor. Finally, consistent with D.98-04-059, the rulings require that TURN, Greenlining, LIF and Public Advocates address underrepresentation, fair determination and duplication in any subsequent compensation request. We affirm these preliminary rulings.

Section 1804(c) provides that a customer found eligible for an award of compensation may file a request within 60 days following issuance of the final order of the Commission. This is the final order in this proceeding. Thus, eligible intervenors may file a request for an award within 60 days of the date this decision is issued. In addition to any other requirement of the Public Utilities Code or Commission decision, the requests, if made, must comply with the requirements stated in the preliminary rulings (e.g., full justification of compensation claim including hourly rates, number of hours, all expenses; must address underrepresentation, fair determination and duplication).

8. CONCLUSION

Merger opponents assert that the proposed merger will create a telecommunications giant that will dominate the market. For the reasons explained above, we disagree. There can be no doubt, however, that the resulting company will be significant in size and reach.

Federal and state authorities could have before now chosen a competitive policy of rejecting nearly all mergers. This could have been a legitimate policy, requiring many relatively smaller firms to produce the competition that is so vital to our economic system. That, however, is not the chosen policy. Rather, mergers and acquisitions are allowed, no matter the size of the resulting company, as long as they meet federal and state guidelines (e.g., economic benefits to ratepayers, not adversely affecting competition, in the public interest).

Moreover, by approving the SBC/Telesis merger, the die was cast. That is, we are on the path of allowing titans to battle it out, along with dozens, if not hundreds, of smaller companies serving niche markets and seeking to become first tier players themselves. There is nothing wrong with this approach. It would, however, be inequitable to be on this path and then deny the GTE/Bell Atlantic merger. Moreover, it would be unreasonable and in conflict with the Public Utilities Code, since the proposed merger meets the requirements in § 854.

There may be a merger that at some point crosses the line and produces a giant that is "too big," with too much "reach," and with a resulting market that is too concentrated, wherein the adverse consequences cannot be mitigated. This is not that merger.

Findings of Facts

1. GTE and Bell Atlantic jointly apply to transfer control of GTE's California utility subsidiaries to Bell Atlantic, which will occur indirectly as a result of GTE merging with Bell Atlantic, with GTE becoming a wholly owned subsidiary of Bell Atlantic, and GTE's California utility subsidiaries becoming second-level subsidiaries of Bell Atlantic.

2. The proposed merger is between two holding companies that do not have any material overlapping operations in California; the transaction does not involve an operational consolidation of any local telephone operating companies or any subsidiaries; GTE's California utility subsidiaries will continue to provide services under the same terms, conditions and regulations that apply prior to the merger, except for the rate reductions that will result from § 854(b)(2); no operations, lines, plant, franchises or permits of regulated subsidiaries will be merged with the lines, plant, franchises or permits of any other regulated public utility, unless such

merger is subsequently approved to the extent required by the Public Utilities Code and the Commission; no changes are planned in the senior management of GTE's California utility subsidiaries; and, from the customer and Commission perspective, the entities that provide services to California customers today will be the same entities providing services after consummation of the merger.

3. In consultation with the Assigned Commissioner, on April 1, 1999, and August 31, 1999, the Presiding Officer preliminarily ruled that TURN, Greenlining, LIF, and Public Advocates are eligible to seek compensation for participation in this proceeding.

4. On September 15, 1999, the California Attorney General filed an Opinion on the competitive effects of the proposed merger in which he finds that the proposed merger will not adversely affect competition.

5. The shareholders of GTE approved the merger on May 18, 1999, and the shareholders of Bell Atlantic approved the merger on May 19, 1999.

6. Applicants' economic benefits proposal was developed by estimating the total amount of expense and capital synergies that GTE and Bell Atlantic jointly expect to achieve across all of their operations, allocating the aggregate estimate between GTE and Bell Atlantic, determining the total amount of net savings attributable to GTE by offsetting merger-related costs, determining the portion of GTE-savings attributable to GTE California, and determining the portion of GTE California-savings attributable to its intrastate Category I and Category II services.

7. Applicants' economic benefits estimate was developed by senior executives from both companies with extensive knowledge of, and experience with, each company's budgets and operations; the estimate was prepared using a collaborative process (the August 21 Group); and some of the executives involved had previous experience in estimating and tracking merger savings, making them particularly well-qualified to develop the savings estimate here.

8. Applicants' economic benefits estimate was developed for presentation to diverse groups, including shareholders, employees, and the investment community, such that applicants had an incentive to neither understate, nor overstate, their estimate.

9. As a percentage of the companies' combined expense bases, GTE and Bell Atlantic's savings estimate is in line with the savings estimated in the mergers of SBC/Telesis and SBC/Ameritech, and applicants' G&A savings estimate as a percentage of their combined operating expenses is in line with similar estimates for nine electric utility mergers.

10. The timing of the other mergers and studies with updated estimates and results (e.g., Bell Atlantic/NYNEX, SBC/Telesis, SBC/Ameritech), as well as the fact Bell Atlantic executives agreed to increase the estimate here to $2.0 billion, show that the August 21 Group had the opportunity to take advantage of experience, and did so.

11. Applicants' savings estimate is consistent with the revised estimate for the Bell Atlantic/NYNEX merger, with expense and capital synergies as a percent of combined operating expenses of 5.6% compared to 6.1%, respectively.

12. Mercer data show that the $2 billion estimated expense savings for the GTE/Bell Atlantic merger compares favorably to updated and revised estimated expense savings in telecommunications mergers between SBC/Telesis, Bell Atlantic/NYNEX, and SBC/Ameritech, with savings as a percent of expenses of 6.1%, 7.2%, 5.8% and 6.0% respectively.

13. GTE is not necessarily more inefficient that other companies.

14. Expenses and expenses per access line may generally reflect efficiency, but also reflect other factors, such that the differences in cost between companies due to rural versus urban service areas, relative age of plant, relative penetration of the latest technologies, and relative mix of customers.

15. Applicants adjusted their economic benefits estimate for pension cost savings, and updated allocation factors, in response to the direct testimony of protestants.

16. As updated, applicants' economic benefits estimates are the best information in this record, except for the matter of whether or not to include revenue synergies, and the definition of the long-term.

17. Benchmarks from other mergers are not determinative of the amount of savings achievable in this proposed merger since companies are unique, and offer different levels of efficiencies and opportunities when they merge.

18. The benchmarks of economic savings from other mergers demonstrate that applicants' estimate is within a reasonable range.

19. The Mercer study states that the total expense savings are $2 billion, including best practices, and does not show a total of $2.6 billion in expense savings.

20. Applicants' estimate of expense savings is $2 billion, not $2.6 billion.

21. Applicants allocated joint savings to affiliates and business units by using allocation methods that GTE employs today, which are consistent with the cost allocation methods routinely used by Bell Atlantic.

22. For regulated telephone operations, GTE's share of joint savings was determined based on the percentage relationship of GTE regulated telephone operations for the "big three expenses" (i.e., plant specific, plant non-specific and customer operations) compared to the same big three expenses for GTE and Bell Atlantic combined. Based on 1998 expense data, this results in 33% of the savings being allocated to GTE, and 67% being allocated to Bell Atlantic.

23. For G&A savings, applicants used the percentage relationship of GTE's total operating expenses and taxes to the total operating expenses and taxes of GTE and

Bell Atlantic combined. Based on 1998 expense data, this results in 45% of G&A savings being allocated to GTE, and 55% being allocated to Bell Atlantic.

24. Capital synergies were identified for telephone operations, long distance, wireless and internet business units and were allocated using the big three expense allocator.

25. Applicants' cost and savings allocation method reflects the extent to which the two companies today consume centrally provided services.

26. GTE's merger with Contel provided GTE some of the same opportunities and benefits that Bell Atlantic enjoyed from its merger with NYNEX.

27. In 1992 GTE initiated a 5-year Process Re-Engineering Program which resulted in GTE changing the way it does business and achieving cost savings.

28. The two types of costs that will be incurred to consummate the merger and integrate the two companies (transaction costs and implementation costs) were developed by applicants' senior executives taking into account the nature of the transaction and their knowledge of the two companies' operations.

29. Applicants directly assign transaction and implementation costs where possible, with remaining costs allocated by the same methodology used to allocate cost savings.

30. A significant part of transaction costs are costs that GTE, and GTE alone, will incur, and are not jointly incurred costs that should be allocated between companies.

31. Merger-caused transaction and implementation costs include such items as professional fees, investment banker fees, regulatory fees, and employee related expenses (e.g., retention, relocation, severance) that are in the nature of expenses, not capital items.

32. The net present value methodology sufficiently takes the timing of costs and benefits into account such that no further amortization of costs or benefits is necessary.

33. The Commission considered but declined to adopt an amortization of merger-related costs in the SBC/Telesis merger decision.

34. Cost savings are an economic benefit by increasing net revenues and profits, and revenue synergies are an economic benefit by increasing net revenues and profits.

35. The Joint Proxy Statement cites significant revenue synergies as one reason that the GTE Board of Directors recommended shareholders vote in favor of the merger, citing annual revenue synergies (increases) at the same $2 billion level as annual expense synergies (decreases).

36. Revenue synergies are the revenues enhancements from the sale of additional vertical services attributable to GTE California.

37. GTE California's penetration rates for vertical services are higher than Bell Atlantic's penetration rates, except for Auto Call Return (Star 69), and only the lower penetration rate for auto call return provides an opportunity within California for revenue enhancement by bringing the rate up to that of Bell Atlantic.

38. Increasing the penetration rate for GTE California to that of Bell Atlantic for Auto Call Return (Star 69) will enhance revenues in California by $2.375 million over 4 years.

39. The level of competition is among the principal factors in defining the long-term, and applicants face the likelihood of robust competition within GTE California's markets given that technology, the industry, the market, and regulation are changing.

40. The extent of competition is not limited to CLEC interconnections, but competitors are developing capabilities to bypass GTE California's network via

direct access, cable telephony, and wireless facilities, with technology convergence becoming an increasingly important factor.

41. Facilities bypass requires time to become an effective competitive alternative.

42. Applicants' financial experts estimated the benefits of the merger over a period of 15 years.

43. Applicants agree to fund the CCA over a period of 10 years.

44. Increased unpredictability requires using more years in the definition of the long-term to ensure that ratepayers receive their share of total economic benefits

45. The state of regulation and ratemaking is another factor in determining the long-term, and this factor supported 5.6 years in the SBC/Telesis merger decision.

46. GTE does 5-year strategic plans.

47. AT&T's Chairman Armstrong says the convergence of technology will happen in 5 years.

48. The long term found in other mergers has tended to be about 5 years.

49. A reliable forecast can be made of economic benefits for 5 years using elements of the analysis from applicant's financial advisors.

50. Applicants' financial analysts estimate a nominal perpetual synergy growth rate of 1% to 3%, the mid-point of which is 2%.

51. Total economic benefits from this proposed merger are $168.1 million (NPV), calculated by adding the revenue synergy benefits over 4 years to applicants' estimates of merger savings over 4 years, escalating the year 4 results to year 5 by 2% (the mid-point of the nominal perpetual synergy growth rate), and using a 10.5% discount rate.

52. The CCA improves on the CPC in ways that support its adoption and funding by ratepayers, such as the CCA providing for the appointment of a third party administrator selected through a request for proposal process within a specific amount of time.

53. Similar to the CPC, the CCA will promote access to telecommunications services in traditionally under-served communities; promote telecommunications and information services projects in the areas of education, literacy, telemedicine, and economic development in those communities; promote universal service by working toward achieving a 98% penetration rate; promote diversity in employment and contracting; and further the Commission's goal of ensuring that California's under-served communities have reasonable access to evolving telecommunications services.

54. The CCA leverages ratepayer funds of $28.9 million (nominal dollars; $19.8 million (NPV)) by applicants agreeing to contribute an additional $4.36 million (nominal dollars), or 15% more, from shareholders.

55. The cost of the CCA to ratepayers is 7 cents per residential customer per month, and 19 cents per business customer per month.

56. The CCA furthers applicants' efforts in the areas stated in the agreement, and goes beyond levels that would exist without the CCA.

57. Pacific serves the majority of the state's telephone customers, while GTE California serves 20% or less of the state's access lines.

58. A benefit provided by the CPC to California under Pacific's program is more likely to be coincident with Pacific's ratepayers than a benefit provided to California under the CCA, unless benefits under the CCA are more narrowly focused.

59. Good faith and intentions are not enough to justify allocating $19.8 million (NPV) of merger benefits to fund the CCA that would otherwise be given directly to ratepayers.

60. A workplan is necessary to reach CCA goals.

61. Effective oversight of the CCA includes measuring success against goals and benchmarks.

62. Applicants have only 1 of 3 positions on the Selection Committee.

63. There is value in having Commission oversight of the Selection Committee and the CCC when money that would otherwise be allocated to ratepayers is involved.

64. Excluding residential monthly service charge revenues from the surcredit billing base means residential access line customers who do not use other services widely will benefit less on a total bill basis than customers with charges for high usage, toll or vertical services, and will also benefit less than will business customers.

65. As of February 1999, a significant number of customers rarely, if ever, make intraLATA toll calls, and only a small percentage use custom calling features.

66. The residential basic exchange rate was included in the billing base for the merger surcredit adopted in the SBC/Telesis decision, and including basic residential access charges in the billing base will not pose problems for calculating the ULTS and CHCF-B funds.

67. Total economic benefits of the proposed merger are $168.1 million (NPV), 50% of which allocated to ratepayers is $84.1 million (NPV), with $64.3 million (NPV) remaining after funding $19.8 million (NPV) for the CCA.

68. The merged company intends to compete for as many California residential customers as it can in as short a timeframe as possible.

69. The proposed merger will foster competition in the long distance and data markets by enabling GTE to expand its GNI in ways that it otherwise would not.

70. The merger will not endanger competition in the market for internet services.

71. Relevant markets include retail and wholesale markets for local exchange, intraLATA toll, interLATA toll, switched access, digital subscriber line, internet, and wireless markets within California, and the national market.

72. GTE and Bell Atlantic do not simultaneously offer retail and wholesale local exchange, toll, switched access, xDSL, internet, and wireless services in California, with the exception of 440 California resale long distance customers of Bell Atlantic.

73. The proposed merger will not adversely affect competition in the local and state markets.

74. The DOJ has withdrawn its opposition to the merger based on applicants' agreeing to sell overlapping wireless properties outside California.

75. With the exception of 440 resale long distance customers, Bell Atlantic is not an actual competitor of GTE in any California market, and elimination of Bell Atlantic as an actual competitor in the long distance market would be competitively insignificant.

76. An actual potential competitor is a firm that does not currently compete in the relevant market but which would enter sometime in the near future, either independently or in combination with another entity in a toehold acquisition.

77. GTE California's local exchange market is now concentrated.

78. The intraLATA toll market in California is now largely competitive.

79. The alleged national market is not now concentrated, and this proposed merger may actually have the effect of reducing concentration within this alleged national market.

80. No documents show that Bell Atlantic has specific plans to enter any California market absent the merger with GTE.

81. Bell Atlantic has no California network facilities from which to supply service, has virtually no customer base from which to initiate a local offering, has limited marketing presence, has limited brand-name recognition, and has no experience supplying local service in California.

82. Bell Atlantic's experience competing in the long distance market out-of-franchise has been "very sobering" and "dismal," even in areas much closer to Bell Atlantic's franchise territories.

83. Bell Atlantic has limited resources and has to prioritize its investments.

84. There are many other firms that are as ready, willing and able as Bell Atlantic to enter California, including into GTE California's service area.

85. Entry by Bell Atlantic would not carry a substantial likelihood of ultimately producing deconcentration or other pro-competitive effects, given its lack of facilities, virtually no customer base, and little brand-name recognition.

86. Bell Atlantic is not an actual potential competitor of GTE in California.

87. We considered and rejected price discrimination and price squeeze arguments in the SBC/Telesis merger.

88. The price squeeze argument is not merger related, but is a problem IECs have with ILECs being able to offer interLATA services before access charges are reformed.

89. To the extent there is an incentive to engage in a price squeeze, GTE has the same incentive even without the merger because GTE already provides interLATA service.

90. The most likely result of an attempted price squeeze would be to replace one IEC with another, and applicants have no conceivable incentive to achieve such a result.

91. Access charges, as are all rates, are set to balance many different and often competing objectives and criteria.

92. A merger application is not the proceeding to address the many complex issues that surround access charges.

93. There is already more competition for large business customers than for any other class of customers.

94. Large business customers are among the most sophisticated of customers in purchasing telecommunications services.

95. The additional competition that will occur as applicants try to secure large business customers will be healthy.

96. GTE California has entered into 56 interconnection agreements, with others pending approval, and it has 249 completed or pending collocation agreements in 80 GTE California central offices, allowing competitors to reach 62% of GTE California's access lines.

97. GTE has established a web-based Wholesale Internet Service Engine to simplify and expedite service ordering and access to OSS, and GTE provides CLECs with information guides, training programs, and help desks, plus staff to visit CLEC sites to help CLECs resolve technical problems.

98. The opening of markets, along with regulatory oversight and facilities bypass, severely limit, if not eliminate, the ability of GTE California to discriminate against, or exclude, competitors.

99. It is exceedingly difficult for an ILEC, including GTE California, to degrade the quality of service on some lines without simultaneously degrading the quality of service it provides to its own customers.

100. Sprint's examples of non-price discrimination do not support conditioning or denying the merger.

101. The merger will combine two holding companies, the ILEC affiliates of GTE and Bell Atlantic will remain as separate corporate entities, and GTE California will continue to report separately to this Commission, while Bell Atlantic's ILECs will continue to report separately to other commissions.

102. The merger will not adversely affect competition.

103. The merger will have pro-competitive effects, such as stimulating competition, and will bring benefits to California.

104. GTE and Bell Atlantic are both financially sound companies, and the proposed merger will give the combined company even more financial resources and flexibility.

105. The proposed merger will not only maintain, but will improve, the financial condition of GTE's California utility subsidiaries.

106. The quality of service experienced by GTE's California customers will be maintained or improved given that the merger is taking place at the level of the parent holding companies, increasing competitive pressures will make providing quality service a business imperative, there is no indication that the merged entity will change the practice of each company tying executive compensation directly to indices of service quality, and applicants are committed to adopting each other's best practices.

107. Applicants must achieve several things, including best practices, to fund the $84.1 million (NPV) allocation of merger benefits to ratepayers.

108. Applicants have committed to maintaining or improving service quality as part of the CCA.

109. Applicants agree to ORA's recommended additional service quality reporting requirements, which further demonstrates applicants' commitment to maintaining or improving service quality.

110. The merger will not adversely affect the quality of service provided to GTE California's wholesale customers given that applicants have committed to a Change Management Process, CLECs will have the opportunity to be involved in any changes applicants make, applicants have committed to maintaining quality of service to wholesale customers, and applicants will be subject to the Commission's OSS requirements and performance measures.

111. The proposed merger will maintain or improve the quality of service to public utility ratepayers in the state.

112. The current management of both GTE and Bell Atlantic are qualified to manage California utility operations, and the combined management will be as well.

113. The proposed merger will maintain or improve the quality of management of the resulting public utilities doing business in the state.

114. GTE has made commitments to its employees to ensure that the proposed merger is fair and reasonable, including a commitment to maintain the level of pension benefits for five years, and to maintain the GTE Savings Plan 401(k) and current severance programs for at least one year.

115. The Communications Workers of America and the California Labor Federation, AFL-CIO have each expressed their support for the proposed merger.

116. No employee or employee group testified to any concern that the proposed merger would be unfair or unreasonable to either union or nonunion employees.

117. The proposed merger will be fair and reasonable to affected public utility employees, including both union and nonunion employees.

118. The shareholders of both companies overwhelmingly approved the proposed merger, and no party asserts that the proposed merger is not fair and reasonable to the majority of affected shareholders.

119. The proposed merger will be fair and reasonable to the majority of all affected public utility shareholders.

120. State and local economies, and the communities served by the merged company, will obtain benefits from the proposed merger through rate reductions, the CCA, allowing the merged company to become a more effective competitor in various telecommunications markets in California, the development of more choices for California ratepayers, the stimulation of competition, increased prospects for growth, increased employment opportunities, and the potential for increased tax revenues.

121. The proposed merger will be beneficial on an overall basis to state and local economies, and to the communities in the area served by the resulting public utility.

122. The proposed merger will preserve the jurisdiction and capacity of the Commission to effectively regulate and audit public utility operations in the state.

123. We now share public data with any other regulatory agency at their request, and will continue to do so.

124. The proposed merger, subject to limited conditions and clarifications, is, on balance, in the public interest.

125. The record does not demonstrate that a no merger alternative produces comparable savings while avoiding possible adverse consequences.

Conclusions of Law

1. Pursuant to § 854(e), applicants must prove by a preponderance of the evidence that the proposed merger meets the requirements for approval in § 854(b) and (c).

2. Applicants' development of economic benefits, including cost allocations and expensing costs as they occur, is reasonable, except for whether to include revenue synergies, and the definition of the short- and long-term.

3. Section 854(b)(2) does not require that benefits allocated to ratepayers be distributed only by surcredits.

4. Nothing in § 854(b)(2) limits the definition of economic benefits to exclude revenue synergies.

5. A reasonable estimate of merger revenue synergies for GTE California is $2.375 million over 4 years.

6. It is reasonable in this proposed merger proceeding to define the short-term as up to five years, and the long-term as five years.

7. A reasonable estimate of total economic benefits of this proposed merger is $168.1 million (NPV), using 5 years for the long-term, and 10.5% for the discount rate.

8. A reasonable allocation of total economic benefits to ratepayers is 50%, or $84.1 million (NPV).

9. The benefits of the CCA, along with the leveraging of ratepayer funds with additional funds from shareholders, make reasonable its adoption, and the funding of $19.8 (NPV) million by ratepayers.

10. Benefits allocated to ratepayers should be used to fund the CCA ($19.8 million (NPV)), with the remainder ($64.3 million (NPV)) returned to ratepayers by a surcredit of $19.0 million each year for 5 years.

11. Funds awarded under the CCA should be spent for activities meeting CCA goals within, to the extent possible, the existing GTE California service area.

12. Applicants should develop a specific workplan, including standards and benchmarks, for the entire CCA; seek adoption of the workplan by majority vote of the CCC; file and serve the workplan in this proceeding (with a copy served on the Director of the Telecommunications Division); and include comparisons of CCA performance against workplan standards and benchmarks in annual reports to the Commission.

13. A member of the Commission staff should be notified of, and entitled to attend each meeting (including executive sessions) of the CCA Selection Committee, and the CCC.

14. The CCC should establish standards for use by the fund administrator in awarding grants to applicants of Community Collaborative Fund resources. The fund administrator, not the CCC, should make the actual grantee selections.

15. Unspent CCA funds, if any, that are funded from the benefits allocated to ratepayers should be returned to ratepayers. Should any funds remain

undistributed within the time period for those funds (e.g., 3 years for universal service, 4 years for contributions, 4 years for technical assistance, 10 years for Community Collaborative Fund), applicants should submit an advice letter to the Commission identifying the amount of unspent funds, and state a recommendation for their distribution.

16. Applicants should serve an advice letter on the Commission, with service on the service list for this proceeding and the Director of the Telecommunications Division, within 60 days of the following relevant periods: if the CCC has not selected a fund administrator and initial funds actually disbursed within 12 months of initiation of the CCA; if initial funds have not been distributed for universal service within 12 months of January 1, 2000; if approximately an additional $1 million has not been spent on contributions within 12 months of initiation of the CCA; and if approximately an additional $90,000 has not been spent on technical assistance within 12 months of initiation of the CCA. The advice letter should identify the problems causing a delay, and state a recommendation.

17. If applicants withdraw for any reason from their CCA financial commitment (including shareholder funds for contributions and technical assistance), the balance of the $19.8 million should be distributed through a billing surcredit over the remainder of the life of the existing surcredit or other reasonable means. Applicants should serve an advice letter within 60 days of any such withdrawal stating the situation and their recommendations.

18. It is reasonable to include annual revenues from the basic residential monthly service charge in the billing base for the surcredit.

19. Applicants should reduce GTE California's annual revenues by $19.0 million each year for five years; should include this revenue reduction in the first October 1 NRF price cap advice letter filing made after consummation of the merger; should include this revenue reduction in each subsequent NRF price cap filing such that

revenue reductions occur over five years; should apply the revenue reduction to a total annual billing base that includes local, toll and access services in effect at the time of the price cap filing, with the billing base incorporating the amounts of both the CHCF-B fund and annual total revenues from residential exchange service access charges; and should state and update the billing base with each advice letter.

20. It is reasonable to expect applicants to honor their intention and commitment to begin business and residential service to the fullest extent possible in San Francisco, Los Angeles, and San Diego within 18 months of merger consummation, and for applicants to submit a report on this within 20 months.

21. The DOJ has concluded that the merger poses no antitrust concerns in any geographic or product market, with the exception of some overlapping wireless properties outside California which applicants have agreed to sell.

22. To prove a loss of actual potential competition, one must establish that: (1) the relevant market is concentrated; (2) but for the merger, the acquiring firm would likely have entered the market in the near future either on its own or by toehold acquisition; (3) there must be few other potential entrants with comparable advantages; and (4) such market entry would carry substantial likelihood of ultimately producing deconcentration of the market or other significant pro-competitive effects.

23. For the potential entrant firm to be considered an actual potential competitor, there must be substantial evidence of a reasonable probability that entry would be in the near future.

24. Even if the acquiring firm would have entered independently or in combination with another entity without the merger, the presence of many other firms which are equally ready and willing to enter makes the issue of actual potential competition moot.

25. The Opinion of the Attorney General does not confuse the law and misapply the burden of proof.

26. The clear majority of the Attorney General's Opinion relies on evidence and argument in this case, Commission decisions, the Public Utilities Code, court decisions, and the Act, all of which we may rely on in reaching our decision.

27. Parties were not deprived of due process with respect to the Attorney General's Opinion, parties addressed the Attorney General's Opinion in their reply briefs, and we consider their comments in determining the appropriate weight to give the Opinion.

28. The recommendation of ORA regarding additional service quality reports, which is agreed to by applicants, should be adopted.

29. GTE and Bell Atlantic, along with their California public utility operating subsidiaries, will continue to be subject to the Public Utilities Code, Commission decisions, Commission General Orders, as well as Commission rules, policies, and practices, whether or not the merger is approved and consummated, regardless of the parent company, and regardless of where the parent company is located.

30. The approval here should be of applicants' request, and not of any other form of approval, except the clarifications and conditions attached to approval.

31. Applicants have met their burden of proof by a preponderance of the evidence that the proposed merger satisfies the conditions in § 854 (b) and (c).

32. The preliminary rulings on intervenor compensation of the Presiding Officer should be affirmed, and TURN, Greenlining, LIF and Public Advocates should each be authorized to file a request for intervenor compensation within 60 days of the date this order is issued.

33. This order should be effective immediately to allow applicants to proceed with consummation of the merger, and the sharing of merger benefits with ratepayers, as soon as possible.

ORDER

IT IS ORDERED that:

1. The joint application of GTE Corporation (GTE) and Bell Atlantic Corporation (Bell Atlantic; collectively applicants) to transfer control of GTE's California utility subsidiaries to Bell Atlantic, which will occur indirectly as a result of GTE merging with Bell Atlantic (wherein GTE will become a wholly owned subsidiary of Bell Atlantic, and GTE's California utility subsidiaries will become second-level subsidiaries of Bell Atlantic), is granted subject to the terms set forth herein, and, if applicants implement the authorized transfer of control, then:

   a. Applicants shall allocate short-term and long-term economic benefits of $84.1 million (net present value) to GTE's California utility ratepayers. Of this amount, $19.8 million (net present value) shall be used to fund the Community Collaborative Agreement (CCA; see Attachment C). The remainder shall be returned to the ratepayers of GTE California Incorporated (GTE California), or any successor to GTE California, by surcredits over 5 years.

   b. GTE California, or its successor, shall reduce its annual revenues by $19.0 million per year for five years. GTE California, or its successor, shall include this revenue reduction in the first October 1 new regulatory framework price cap advice letter filing made after consummation of the merger. GTE California, or its successor, shall include this revenue adjustment in each October 1 price cap advice letter filing for a total of five years. Each price cap advice letter shall specify, among other things, the billing base for the purpose of this surcredit. The billing base shall include local, toll and access service revenues, with the billing base incorporating the amount of both the CHCF-B and the annual total revenues from residential exchange service access charges. The billing base shall be updated with each price cap advice letter.

c. Applicants shall implement the CCA, subject to the following clarifications regarding our approval:

   i. All funds awarded under the CCA (including those funded both by ratepayers and shareholders) should be spent for activities meeting CCA goals within the existing GTE California service area, to the extent possible.

   ii. Applicants shall develop a specific workplan, including standards and benchmarks, for the entire CCA within 120 days of consummation of the merger. The workplan shall include a statement showing applicants actual California philanthropic contributions for the last five years. Applicants shall seek adoption of the workplan by majority vote of the Community Collaborative Committee (CCC). Whether or not adopted by the CCC, applicants shall file and serve the workplan in this proceeding as a compliance filing, with a copy served on the Director of the Telecommunications Division. Except for service on the Commission, service may be by Notice of Availability, even if the workplan is less than 75 pages. (Rule 2.3 of the Commission's Rules of Practice and Procedure.) Parties shall have 20 days to file and serve responses, with a copy served on the Director of the Telecommunications Division. Applicants shall have 5 days to file and serve a reply. The Director of the Telecommunications Division may determine whether or not efforts should be employed by the Commission to resolve differences, if any.

   iii. Applicants shall serve an Annual Report regarding CCA activities within 60 days of completion of the first year of the CCA, and each year thereafter, with a copy served on the Director of the Telecommunications Division, and the service list to this proceeding. Except for service on the Commission, service may be by Notice of Availability, even if the Annual Report is less than 75 pages. The Annual Reports shall contain, among other things, the yearly budget, an accounting of expenditures, a listing of projects funded, and an assessment of the success of the CCA compared to applicants' filed workplan.

iv. The Director of the Telecommunications Division (or a person he or she may designate) shall be notified of, and entitled to attend, each meeting (including executive sessions) of the Selection Committee and the CCC, review all communications between members of each committee, review all communications between each committee (or any member of each committee) and any applicant for the position of administrator or applicant for funds, and review all communications between each committee (or any member of each committee) and any other person or entity.

v. The CCC shall establish standards for use by the fund administrator in awarding grants to applicants of Community Collaborative Fund resources. The fund administrator, not the CCC, shall make the actual grantee selections. CCA funds shall be used, to the fullest extent possible, to meet the CCA's objectives (e.g., serving under-served communities), not paying internal operations costs of the recipient organizations. Spending of funds by recipients of CCA awards shall be without restrictions imposed by any signatory to the CCA whose interests may be different from those of the recipient, except to the extent those restrictions are contained in the overall guidelines adopted by the CCC for use by the administrator in awarding funds. The CCC should ensure that the administrative costs for the entire administration of the CCA are kept to a minimum.

vi. Applicants shall file and serve an advice letter on the Commission, with service on the service list for this proceeding, and service on the Director of the Telecommunications Division, within 60 days of the following relevant periods: if the Selection Committee has not selected a fund administrator and initial funds actually disbursed by the fund administrator within 12 months of initiation of the CCA; if initial funds have not been distributed for universal service within 12 months of January 1, 2000; if approximately an additional $1 million has not been spent on contributions within 12 months of initiation of the CCA; and if approximately an additional $90,000 has not been spent on technical assistance within 12 months of initiation of the CCA. The advice letter shall identify the problems causing a delay, and state a recommendation. Parties shall have 20 days to serve comments or protests, and applicants shall have 5 days to serve a response. The Director of the Telecommunications Division shall review the advice letter, comments, protests, and response, if any, and prepare a resolution for our consideration. The resolution shall adopt applicants' recommendation, adopt a reasonable alternative, or set the matter for formal consideration.

vii. Unspent CCA funds, if any, that are funded from the benefits allocated to ratepayers shall be returned to ratepayers. Should any funds remain undistributed within the time period for those funds (e.g., three years for universal service, four years for contributions, four years for technical assistance, 10 years for Community Collaborative Fund), applicants shall, within 60 days after expiration of the period, file and serve an advice letter with the Commission, with service on the service list for this proceeding and on the Director of the Telecommunications Division. The advice letter shall identify the amount of unspent funds, and state a recommendation for their distribution. Parties shall have 20 days to serve comments or protests, and applicants shall have 5 days to serve a response. The Director of the Telecommunications Division shall review the advice letter, comments, protests, and response, if any, and prepare a resolution for our consideration. The resolution shall adopt applicants' recommendation, adopt another distribution of the funds, set the matter for formal consideration, or otherwise reasonably address the matter.

viii. If applicants withdraw for any reason from their CCA financial commitment (including shareholder funds for contributions and technical assistance), the balance of the $19.8 million (net present value) of benefits allocated to ratepayers shall be distributed to ratepayers through a billing surcredit over the remainder of the life of the existing surcredit, or other reasonable means. Applicants shall serve an advice letter within 60 days of any such withdrawal, subject to the same process as explained above for comments, protests, response, and a resolution for our consideration.

d. Applicants shall file a report with the Director of the Telecommunications Division, with service on the service list for this proceeding, within 20 months of consummation of the merger. The report shall show applicants' success in having begun serving customers in San Francisco, Los Angeles, and San Diego within 18 months of merger consummation, and further show applicants' progress towards serving residential customers in these and other markets. The report shall explain applicants' plans to meet their commitments if they have not been met within 18 months, or explain their reasons for changing their goals if these goals have changed. Other than service on the Commission, service may be by Notice of Availability, even if the report is less than 75 pages.

e. Applicants shall serve the service quality reports specified in Attachment D.

2. Applicants shall file and serve a written notice in this proceeding of their agreement to the transfer of control and merger of their companies consistent with the terms set forth in this order. The agreement shall be evidenced by a resolution of their respective Boards of Directors authenticated by an appropriate corporate officer. The authority to transfer control and merge granted herein shall expire 90 days from the effective date of this order if applicants fail to file an authenticated resolution of their agreement with the terms of this order within 90 days from today. The authority to transfer control and merge granted herein shall expire

365 days from the effective date of this order if applicants fail to transfer control and merge as authorized herein within 365 days from today.

3. Within 30 days of the issuing date of any decision by another jurisdiction which materially changes the terms of the proposed transaction as it affects any of applicants' California utility operations, applicants shall file and serve a copy of that decision in this proceeding, with a copy on the service list and the Director of the Telecommunications Division. The filing shall also include an analysis of the impact of any terms and conditions contained therein as they affect any of applicants' California utility operations.

4. Applicants shall notify the Commission, with a copy served on the service list for this proceeding and the Director of the Telecommunications Division, of the date the merger is consummated. The notice shall be served within 15 days of merger consummation.

5. In the event that the books and records of applicants or any affiliates thereof are required for inspection by the Commission or its staff, applicants shall either produce such records at the Commission's offices, or reimburse the Commission for the reasonable costs incurred in having Commission staff travel to any of applicants' offices.

6. If applicants consummate the proposed merger authorized herein, their failure to comply with any element of this order shall constitute a violation of a Commission order, and subject applicants to penalties and sanctions consistent with law.

7. The following intervenors may file a request for an award of intervenor compensation within 60 days of the date this order is issued: The Utility Reform Network, Greenlining Institute, Latino Issues Forum, National Council of La Raza, Southern Christian Leadership Conference, Filipinos for Affirmative Action, Filipino Civil Rights Advocates, Korean Youth and Community Center, California

Rural Indian Health Board, Association of Mexican American Educators, California Association of Asian-Pacific Bilingual Education, and California Association for Bilingual Education. In addition to any other requirements of the Public Utilities Code or Commission decisions, any request, if made, shall comply with the requirements stated in the April 1, 1999, and August 31, 1999, Preliminary Rulings of the Presiding Officer.

8. This proceeding is closed.

This order is effective today.

Dated March 2, 2000, at San Francisco, California.

RICHARD A. BILAS
President
HENRY M. DUQUE
JOSIAH L. NEEPER
Commissioners

I dissent.

/s/ CARL W. WOOD
Commissioner

I dissent.

/s/ LORETTA M. LYNCH
Commissioner

************ SERVICE LIST *************

Last updated on 03-MAR-2000 by: SMJ
A9812005 LIST

***************** APPEARANCES *****************

Evelyn K. Elsesser
ALEXIS WODTKE
Attorney At Law
ALCANTAR & ELSESSER LLP
ONE EMBARCADERO CENTER, STE 2420
SAN FRANCISCO CA 94111
(415) 421-4143
eke@aelaw.com
For: SPRINT COMMUNICATIONS LLP

Joseph S. Faber
Attorney At Law
AT&T
1350 TREAT BLVD., SUITE 500
WALNUT CREEK CA 94596
(925) 949-0698
jsfaber@att.com
For: AT&T COMMUNICATIONS OF CALIFORNIA, INC.

Randolph W. Deutsch
Attorney At Law
AT&T COMMUNICATIONS OF CALIFORNIA, INC.
795 FOLSOM STREET, 2ND FLOOR
SAN FRANCISCO CA 94107
(415) 442-5560
deutsch@att.com
For: AT&T COMMUNICATIONS OF CALIFORNIA, INC.

John M. Walker
Regulatory Counsel
BELL ATLANTIC CORPORATION
1710 H STREET, N.W.
WASHINGTON DC 20006
(202) 392-5296
john.m.walker@bellatlantic.com
For: BELL ATLANTIC CORPORATION

Susan E. Brown
Attorney At Law
LATINO ISSUES FORUM
785 MARKET STREET, 3RD FLOOR
SAN FRANCISCO CA 94103-2003
(415) 284-7224
For: LATINO ISSUES FORUM

Earl Nicholas Selby
Attorney At Law
LAW OFFICES OF EARL NICHOLAS SELBY
418 FLORENCE STREET
PALO ALTO CA 94301-1705
(650) 323-0990
enselby@wenet.net
For: ICG TELECOM GROUP, INC. and NEXTLINK CALIFORNIA

Gregory Bowling
Attorney At Law
MCCUTCHEN DOYLE BROWN & ENERSEN LLP
THREE EMBARCADERO CENTER
SAN FRANCISCO CA 94111
(415) 393-2601
gbowling@mdbe.com
For: AT&T COMMUNICATIONS OF CALIFORNIA, INC.

Matthew S. Gray
Attorney At Law
MCCUTCHEN, DOYLE, BROWN & ENERSEN LLP
THREE EMBARCADERO CENTER
SAN FRANCISCO CA 94111
(415) 393-2256
mgray@mdbe.com
For: COVAD COMMUNICATIONS COMPANY

Kathleen S. Rogers
MCI WORLDCOM
201 SPEAR STREET, 9TH FLOOR
SAN FRANCISCO CA 94105
(415) 228-1471
katy.rogers@mci.com
For: MCI WORLDCOM

Henry Weissmann
HOJOON HWANG
Attorney At Law
MUNGER, TOLLES & OLSON LLP
355 SOUTH GRAND AVENUE, SUITE 3500
LOS ANGELES CA 90071-1560
(213) 683-9150
weissmannhx@mto.com
For: GTE Corporation

Lindsay Bower
Deputy Attorney General
OFFICE OF THE ATTORNEY GENERAL
455 GOLDEN GATE AVE., STE 11000
SAN FRANCISCO CA 94102-3664
(415) 703-5517
bowerl@hdcdojnet.state.ca.us
For: CALIFORNIA DEPARTMENT OF JUSTICE

Peter A. Casciato
Attorney At Law
PETER A. CASCIATO, A PROF. CORP.
8 CALIFORNIA STREET, SUITE 701
SAN FRANCISCO CA 94111-4825
(415) 291-8661
pcasciato@rcn.com
For: MediaOne Telecommunications of CA/NorthPoint Communications

Mark Savage
Attorney At Law
PUBLIC ADVOCATES, INC.
1535 MISSION STREET
SAN FRANCISCO CA 94103-2500
(415) 431-7430
marksavage@igc.apc.org
For: National Council of La Raza

************ SERVICE LIST ************

Christopher Witteman
Attorney At Law
THE GREENLINING INSTITUTE
785 MARKET STREET, 3RD FLOOR
SAN FRANCISCO CA 94103
(415) 284-7202
chrisw@greenlining.org
For: GREENLINING INSTITUTE

Paul Stein
Attorney At Law
THE UTILITY REFORM NETWORK
711 VAN NESS AVENUE, SUITE 350
SAN FRANCISCO CA 94102
(415) 929-8876
pstein@turn.org
For: The Utility Reform Network

Laura J. Tudisco
Legal Division
RM. 5001
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-2164
ljt@cpuc.ca.gov
For: OFFICE OF RATEPAYER ADVOCATES (ORA)

*************** STATE SERVICE ****************

Kelly Boyd
Office of Ratepayer Advocates
770 L STREET, SUITE 1050
SACRAMENTO CA 95814
(916) 327-2453
keb@cpuc.ca.gov
For: Office of Ratepayer Advocates

Charles H. Christiansen
Telecommunications Division
AREA 3-D
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-1901
chc@cpuc.ca.gov
For: OFFICE OF RATEPAYER ADVOCATES (ORA)

Cherrie Conner
Telecommunications Division
AREA 3-D
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-2767
chr@cpuc.ca.gov

Fassil T. Fenikile
Executive Division
RM. 5212
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-1159
ftf@cpuc.ca.gov

William Johnston
Office of Ratepayer Advocates
RM. 4101
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-2256
wej@cpuc.ca.gov

Lorann King
Telecommunications Division
AREA 3-D
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-3473
lor@cpuc.ca.gov

Burton Mattson
Administrative Law Judge Division
RM. 5105
505 VAN NESS AVE
SAN FRANCISCO CA 94102
(415) 703-2504
bwm@cpuc.ca.gov

Barbara Ortega
Executive Division
RM. 500
320 WEST 4TH STREET SUITE 500
LOS ANGELES CA 90013
(213) 576-7070
bho@cpuc.ca.gov

************** INFORMATION ONLY **************

Marc D. Joseph
Attorney At Law
ADAMS BROADWELL JOSEPH & CARDOZO
651 GATEWAY BLVD., SUITE 900
SOUTH SAN FRANCISCO CA 94080
(650) 589-1660
mdjoseph@adamsbroadwell.com
For: COMMUNICATION WORKERS OF AMERICA (CWA)

Alexis Wodtke
Attorney At Law
ALCANTAR & ELSESSER LLP
ONE EMBARCADERO CENTER, STE 2420
SAN FRANCISCO CA 94111
(415) 421-4143
awodtke@aandellp.com

William D. Smith
Regulatory Counsel
BELL ATLANTIC CORPORATION
1095 AVENUE OF THE AMERICAS
NEW YORK NY 10036
(212) 395-6495
william.d.smith@BellAtlantic.com
For: Bell Atlantic Corporation

Heidi Sieck Williamson
Dept Of Telecommunications & Information
CITY & COUNTY OF SAN FRANCISCO
875 STEVENSON STREET, 5TH FLOOR
SAN FRANCISCO CA 94103
(415) 554-0811
heidi_sieck-williamson@ci.sf.ca.us

Jayne Chongsoon Lee
CITY ATTORNEY, CITY/COUNTY SAN FRANCISCO
CITY HALL, ROOM 234
1 DR. CARLTON B. GOODLETT PLACE
SAN FRANCISCO CA 94102-4682
(415) 554-4634
jayne_lee@ci.sf.ca.us
For: City and County of San Francisco

************ SERVICE LIST ************

d Sonnenberg
COVAD COMMUNICATIONS COMPANY
2330 CENTRAL EXPRESSWAY, BUILDING B
SANTA CLARA CA 95050
(408) 844-7504
bsonnenb@covad.com

John L. Clark
KATHRYN A. FUGERE KFUGERE@GMSSR.COM
Attorney At Law
GOODIN MACBRIDE SQUERI RITCHIE & DAY LLP
505 SANSOME STREET, 9TH FLOOR
SAN FRANCISCO CA 94111
(415) 765-8443
jcclark@gmssr.com
For: TELECOMMUNICATIONS RESELLERS ASSOCIATION

Kathryn A. Fugere
Attorney At Law
GOODIN MACBRIDE SQUERI RITCHIE & DAY LLP
505 SANSOME STREET, 9TH FLOOR
SAN FRANCISCO CA 94111
(415) 765-8421
kfugere@gmssr.com
For: Telecommunications Resellers Association

Barry Pineles
Regulatory Counsel
GST TELECOM, INC.
4001 MAIN STREET
VANCOUVER WA 98663
(360) 906-7104
bpineles@gstworld.net

Margo Friedrich
GTE CALIFORNIA INCORPORATED
711 VAN NESS AVENUE, SUITE 300
SAN FRANCISCO CA 94102
(415) 474-4708
margo.friedrich@telops.gte.com

Steven E. Zipperstein
Regional V.P. & General Counsel
GTE CALIFORNIA INCORPORATED
ONE GTE PLACE, CA500LB
THOUSAND OAKS CA 91362-3811
(805) 372-6676
steve.zipperstein@telops.gte.com

Doug Garrett
Senior Director, Government Affairs
ICG COMMUNICATIONS, INC.
180 GRAND AVENUE, STE 800
OAKLAND CA 94612
(510) 239-7089
doug_garrett@icgcomm.com
For: ICG COMMUNICATIONS, INC.

Erin R. Swansiger
KELLEY DRYE & WARREN, LLP
1200 19TH STREET, N.W., SUITE 500
WASHINGTON DC 20036
(202) 887-1232
eswansiger@kelleydrye.com
For: KELLEY DRYE & WARREN LLP

Kim Logue
Regulatory Analyst
LCI INTERNATIONAL TELECOM CORP.
4250 N. FAIRFAX DRIVE, 12W002
ARLINGTON VA 22203
(703) 363-4321
kim.logue@qwest.net

Anthony J. Ditirro
MCI WORLDCOM, INC.
201 SPEAR STREET, 9TH FLOOR
SAN FRANCISCO CA 94105
(415) 228-1900
tony.ditirro@mci.com

Theresa L. Cabral
Senior Corporate Counsel
MEDIAONE TELECOMMUNICATIONS OF CALIF.
1999 HARRISON STREET, STE 660
OAKLAND CA 94612
(510) 273-8685
tcabral@mediaone.com
For: MEDIAONE TELECOMMUNICATIONS OF CALIFORNIA

Hojoon Hwang
Attorney At Law
MUNGER TOLLES & OLSON LLP
33 NEW MONTGOMERY ST., 19TH FLOOR
SAN FRANCISCO CA 94105-9781
(415) 512-4009
hwanghx@mto.com
For: GTE CORP.

Esther Northrup
Attorney At Law
NEXTLINK CALIFORNIA, INC.
5771 COPELY DRIVE
SAN DIEGO CA 92111
(858) 244-4910
ehnorthrup@nextlink.com

Karen M. Potkul
Attorney At Law
NEXTLINK CALIFORNIA, INC.
1924 E. DEERE AVENUE, STE 110
SANTA ANA CA 92705
(949) 417-7766
kpotkul@nextlink.net
For: NEXTLINK CALIFORNIA

Melissa Waksman
Attorney At Law
NEXTLINK CALIFORNIA, INC.
3 WATERS PARK DRIVE, SUITE 100
SAN MATEO CA 94403
(650) 227-5015
mwaksman@nextlink.com

Martin A. Mattes
Attorney At Law
NOSSAMAN GUTHNER KNOX & ELLIOTT, LLP
50 CALIFORNIA STREET, 34TH FLOOR
SAN FRANCISCO CA 94111-4799
(415) 438-7273
mmattes@nossaman.com

************ SERVICE LIST *************

Fredrick Gamble
Consultant
OUTER SPHERE, INC.
1445 CEDAR AVENUE
SAN LEANDRO CA 94579
(510) 351-0518
fredgamble@earthlink.net
For: COX CALIFORNIA TELECOM, LLC

Maria E. Andrade
PUBLIC ADVOCATES, INC.
1535 MISSION STREET
SAN FRANCISCO CA 94103-2500
(415) 431-7430
MariaEAndrade@hotmail.com

Natalie D. Wales
Attorney At Law
SPRINT COMMUNICATIONS COMPANY, L.P.
1850 GATEWAY DRIVE, 7TH FLOOR
SAN MATEO CA 94404-2467
(650) 513-2732
natalie.d.wales@mail.sprint.com

Robert Gnaizda
General Counsel/Policy Director
THE GREENLINING INSTITUTE
785 MARKET STREET, 3RD FLOOR
SAN FRANCISCO CA 94103-2003
(415) 284-7202
robertg@greenlining.org

Robert Finkelstein
Attorney At Law
THE UTILITY REFORM NETWORK
711 VAN NESS AVENUE, SUITE 350
SAN FRANCISCO CA 94102
(415) 929-8876
bfinkelstein@turn.org
For: The Utility Reform Network

M. Carter Delorme
Attorney At Law
WINSTON & STRAWN
1400 L STREET, N.W.
WASHINGTON DC 20005-3502
(202) 371-5956
mdelorme@winston.com
For: Bell Atlantic

(END OF ATTACHMENT A)

ATTACHMENT B
ECONOMIC BENEFITS AND SURCREDIT
($ Millions)

LINE NO.	YEAR	NET SAVINGS[1]	REVENUE INCREMENT[2]	TOTAL SAVINGS	NET PRESENT VALUE FACTOR (10.5%; 1999 = 1.0)	NET PRESENT VALUE OF TOTAL SAVINGS	LEVELIZED REVENUE REDUCTION[3]	NET PRESENT VALUE OF LEVELIZED REVENUE REDUCTION
		(a)	(b)	(c) = (a) + (b)	(d)	(e) = (c) * (d)	(f)	(g) = (d) * (f)
1	2000	($32.5)	$0.2	($32.3)	0.9050	($29.2)	NA	NA
2	2001	33.6	0.5	34.1	0.8190	27.9	19.0	15.6
3	2002	74.1	0.8	74.9	0.7412	55.5	19.0	14.1
4	2003	87.5	0.8	88.3	0.6707	59.2	19.0	12.7
5	2004[4]	89.3	0.8	90.1	0.6070	54.7	19.0	11.5
6	2005	NA	NA	NA	0.5493	NA	19.0	10.4
7	TOTAL					$168.1		$64.3

8	50% to ratepayers (50% of column e, line 7)	$84.1
9	Community Collaborative Agreement	$19.8
10	Net Amount for Surcredit (line 8 minus line 9)	$64.3
11	Levelized for five years at 10.5%[3]	$19.0
12	Surcredit (line 11 over an estimated billing base of $2.0 billion)	0.950%
13	Reduction in Average Monthly Bill[5]	
14	Residential	32 cents per month
15	Business	47 cents per month

NA = not applicable.

[1] Exhibit 37, page 34.

[2] Exhibit 5, page 40.

[3] This amount is the levelized annual revenue reduction beginning in 2001 of which the net present value equals $64.3 million.

[4] Net savings (column a) and revenue increment (column b) are escalated from 2003 by 2%. (Exhibit 157, LSS-1, page I-44; average of synergy growth rate range of 1% to 3%.)

[5] The reduction is based on an average monthly residential bill of $33.18, and an average monthly business bill of $49.20. (Exhibit 33, page 3.)

ATTACHMENT C

GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

This document sets forth the joint proposal of GTE and Bell Atlantic for the adoption of measures to ensure that their merger will promote the interests of California consumers, including those in low-income, ethnic, minority, disabled and limited-English speaking communities of California, in both urban and rural areas. In consideration of the willingness of GTE and Bell Atlantic to adopt and to advance these proposals to the California Public Utilities Commission ("CPUC") and for the ten years of this partnership, the groups listed at the end of this document agree (1) to withdraw their protests to A.98-12-005 if they have filed any protests; (2) to make filings with the CPUC as appropriate expressing their support for the merger with the commitments set forth herein, recommending that the CPUC authorize the adoption of the programs (and associated cost recovery) as set forth herein, and recommending that the CPUC approve the merger without the imposition of additional conditions; (3) not to assist other parties in their efforts to persuade the CPUC to disapprove or to impose additional conditions upon the approval of the merger; (4) to take such further action as may be reasonably necessary to advance the objectives of this agreement.

GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

PREAMBLE

Vast and important changes are taking place in the telecommunications landscape, with important opportunities to serve the needs of all Californians. This Community Collaborative Agreement specifically seeks to ensure that California's traditionally underserved communities, including low-income, ethnic, minority, limited-English-speaking, and disabled communities in California's various rural, urban, and inner-city regions, will benefit fully and equally along with all of California, from these extraordinary changes. GTE/Bell Atlantic and the Community Partners below are particularly committed to ensuring that Californians, including Californians in underserved communities, have full and equal access to telecommunications services as they exist today and as they are evolving into advanced voice, data, video, and wireless networks that can impact profoundly upon the way people work, learn, and live.

Bell Atlantic and GTE have demonstrated a strong commitment to the communities they serve and the core values of customer care and universal service. Accessibility for people with disabilities, racial and ethnic diversity in the workforce and marketplace, consumer protection and education, economic development and creation of new opportunities for small businesses will be hallmarks of the new, combined company.

The merger will promote competition, choice and the rapid deployment of advanced telecommunications technology in all communities served by the new company and beyond. The Community Collaborative Agreement reflects a strategic alliance to promote that vision and leadership. The parties to this agreement believe that California's low-income, minority, limited English-speaking, and disability communities are a critical element of California's future and success, and are equally important markets for GTE and Bell Atlantic.

UNDERSERVED COMMUNITIES OF CALIFORNIA

For purposes of this agreement, California's underserved communities include its low-income, ethnic, minority, limited-English-speaking, and disabled communities in California's various rural, urban, and inner-city regions.

COMMUNITY COLLABORATIVE FUND

GTE/Bell Atlantic will propose to the CPUC that the "Community Collaborative Fund" discussed in its merger application be increased to $25 million over 10 years. A separate third party 501 (c) (3) agency(s) will be contracted to administer the $25 million fund. The funds will be used for underserved community access to telecommunications and information services, education, literacy, telemedicine, economic development and telecommunications advocacy in underserved communities. The parties agree that the $25 million will represent a portion of the merger savings under Public Utilities Code section 854 (b)(2), and that the Community Collaborative fund represents a method of equitably allocating merger savings to ratepayers. A three-person Selection Committee will be formed for the purpose of choosing the Fund Administrator. This Committee will represent all signatories and will be comprised of the following:

GTE/Bell Atlantic	1 Representative
Public Advocates and Non-Intervenor Signatories	1 Representative
Greenlining Institute and Latino Issues Forum	1 Representative

This Selection Committee will meet within 60 days of the CPUC's approval of the merger and will endeavor to select a Fund Administrator, using a competitive request for proposal, within 90 days of the closing of the GTE/Bell Atlantic merger.

COMMUNITY COLLABORATIVE COMMITTEE

For purposes of implementing and monitoring this agreement over the ten years of the collaborative, the signatory community coalitions below and GTE/Bell Atlantic shall each designate a representative to form together the GTE/Bell Atlantic Community Collaborative Committee. This committee shall consider reports from GTE/Bell Atlantic on the progress and results in implementing this agreement and, in collaboration with the ULTS Partnership, shall select 3 additional members to the ULTS Partnership for the Universal Service purposes described herein. The Community Collaborative Committee will not be involved in the distribution of the funds.

MAJOR PRESENCE IN CALIFORNIA

GTE/Bell Atlantic will hold leadership meetings at least semi-annually with the Community Collaborative Committee, community-based organizations and public interest groups. At least once a year this meeting will include the California president and senior management. GTE's CEO will meet with community-based organizations during 1999 to discuss mutual concerns.

UNIVERSAL SERVICE

GTE/Bell Atlantic will commit to working in good faith towards achieving a 98 percent Universal Service goal, with a focus on increasing penetration in California's under-served/underrepresented communities to 98 percent. In order to promote this good faith effort, GTE/Bell Atlantic will continue to support the ULTS Partnership for at least three years beyond 2000. GTE/Bell Atlantic and the partnership will consider other underserved populations (i.e., the disabled and Native Americans) and public communications to ascertain what issues and policies, including a universal design policy and public-interest pay telephones, need to be addressed to advance universal service in those underserved communities. GTE/Bell Atlantic and the partnership will also consider the digital divide between underserved/underrepresented communities and the rest of California. The parties to this agreement will support before the CPUC, GTE/Bell Atlantic's proposal to recognize the three year $1.3 million annual cost of the extension of this program as a method to equitably allocate forecasted economic benefit to ratepayers.

The existing ULTS Partnership will be expanded to include three additional Community Based Organization (CBO) members. The Community Collaborative Committee will recommend new CBOs to the ULTS Partnership.

CONTRIBUTIONS

GTE/Bell Atlantic will increase California's community support, for a minimum of four years, from the existing $2.5 million per year to $3.5 million per year. One hundred percent of the additional $1 million per year will be directed to grants to non-profit community-based organizations serving California's underserved communities. GTE/Bell Atlantic will not propose to offset this increase from merger savings.

TECHNICAL ASSISTANCE

GTE/Bell Atlantic will encourage and support its more than 13,000 California employees to donate their time and knowledge to nonprofit, 501 (c) (3) agencies that have a focus on literacy, education and technology application programs. This support will continue to be in the form of monetary grants to organizations to which employees volunteer their time. GTE/Bell Atlantic will continue to provide assistance to employees and will champion providing this technical assistance to organizations serving underserved communities throughout California. GTE/Bell Atlantic will more than double its budget from $60,000 to $150,000 to support employees in this effort.

QUALITY OF SERVICE

GTE/Bell Atlantic will maintain or improve the quality of telephone service in California including the underserved communities.

DIVERSITY

Employment

GTE/Bell Atlantic is committed to continuing to make diversity a critical component in the recruitment, hiring, career development and promotion of all people including minority, women and disabled employees at all levels. As a business issue, it is critical that we understand the diverse markets we serve. Indeed, our success in effectively meeting the needs of our diverse customers depends in part on our ability to fully utilize the diverse skills and backgrounds of our employees. GTE/Bell Atlantic intends, consistent with the new competitive environment, to maintain and where practical improve representation of minority, women and disabled employees in its California workforce and to be an industry leader in California in the employment and advancement of minorities, women and the disabled throughout its management ranks.

GTE/Bell Atlantic's commitment to employee diversity includes to the following areas:

Hiring and Promoting -- GTE/Bell Atlantic will hire the best people, including those with diverse styles, backgrounds and skill sets.

Education and Training -- GTE/Bell Atlantic will support diversity awareness education and skills training for employees to enhance cross-cultural understanding and build the competencies necessary to manage a diverse workforce, work effectively in diverse teams and advance upward in the organization.

Communication -- Executive leadership will engage in frequent communication about opportunities and issues related to diversity and its importance to GTE/Bell Atlantic's business. They will continue to participate as speakers in GTE/Bell Atlantic training classes and utilize these opportunities to encourage two-way dialogue about critical business issues and diversity's role in achieving the company's strategic vision.

Workforce Development -- GTE/Bell Atlantic will provide employees with the technological tools needed to contribute to the success of GTE/Bell Atlantic and their own careers.

Supplier Contracts

In 1998, GTE California spent 25.97 percent of its vendor dollars on businesses owned by minorities, women and disabled veterans. Following the merger, GTE/Bell Atlantic intends, consistent with the new competitive environment, to make a good faith effort in positioning GTE/Bell Atlantic as one of the industry leaders in contracts to qualified and competitive minority vendors as defined by the CPUC and GO-156.

Moreover, GTE/Bell Atlantic is committed to fostering business practices that support and value diversity in community and supplier relations, with the intent of providing equal opportunity and creating economic development among populations that need it most.

MEDIA

All parties agree to jointly develop a communication strategy, including a media and community announcement (s), concerning this GTE/Bell Atlantic Community Collaborative Agreement.

COUNTERPARTS

This agreement may be executed in counterparts and shall be binding as to each signatory as of the date executed by such signatory.

SUMMARY OF GTE/BELL ATLANTIC
COMMUNITY INVESTMENT
(Nominal $ in millions)

Community Collaborative	$25.0
ULTS Extension	$ 3.9
Community Support	$ 4.0
Employee Volunteer Program	$ .4
Total Community Investment	**$33.3**

SO AGREED:

GTE CORPORATION

By: /s/ David R. Bowman Date: 6/15/99
David R. Bowman
President-GTE California

BELL ATLANTIC CORPORATION

By: /s/ Suzanne A. DuBose Date: 6/18/99
Suzanne A. DuBose
President-Bell Atlantic Foundation

GREENLINING INSTITUTE

By: /s/ John Gamboa Date: 6/18/99
John Gamboa
Executive Director

LATINO ISSUES FORUM

By: /s/ Viola Gonzales Date: 6/16/99
Viola Gonzales
Executive Director

PUBLIC ADVOCATES, INC.

By: /s/ Mark Savage Date: 6/16/99
Mark Savage
Managing Attorney

On behalf of itself and the following organizations:

Association of Mexican American Educators
California Association for Asian-Pacific Bilingual Education
California Association for Bilingual Education
California Rural Indian Health Board
Filipino Civil Rights Advocates
Filipinos for Affirmative Action
Korean Youth and Community Center
National Council of La Raza
Southern Christian Leadership Conference

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED

AFRICAN AMERICANS FOR TELECOMMUNICATIONS EQUITY

By: /s/ Gwen Moore Date: 6/15/99
The Honorable Gwen Moore
Chair

On behalf of itself and the following organizations:

Allen Temple Institute for Social Justice
Breakaway Technologies, Inc.
California African American Leadership Institute
Community Education Organization, Inc.
Council of Black Administrators
Creative After School Alternatives
First A.M.E. Renaissance
Inter-Faith Ministers Coalition
KPOO-FM Radio
L.A. Sports Academy
Say Yes, Inc.
Urban Economic Development Corporation
West Coast Black Publishers Association
Western Council on Educating the Black Child
Women's Economic Agenda Project
Yes To Jobs
Ed Alston (individual)
Carol Cody (individual)

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

ALLIANCE FOR PUBLIC TECHNOLOGY

By: /s/ Barbara O.'Connor, Ph.D. Date: 6/16/99
Barbara O'Connor
Founder

On behalf of itself and the following organizations:

The Alliance for Public Technology (APT) is a non-profit organization of more than 300 public interest groups and individuals. APT's members work together to foster broad band access to affordable, usable information and communication services and technology for the purpose of, for example, bringing better and more affordable health care to all citizens, expanding educational opportunities for lifelong learning, enabling people with disabilities to function in ways they otherwise could not, creating opportunities for jobs and economic advancement, and making government more responsive to all citizens.

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

ASIAN PACIFIC AMERICAN COMMUNITY PARTNERSHIP

By: /s/ Anni Chung Date: 6/15/99
Anni Chung
Co-Chair

By: /s/ Tessie Guillermo Date: 6/15/99
Tessie Guillermo
Co-Chair

On behalf of itself and the following organizations:

ASIAN, Inc.
Asian Law Caucus
Asian & Pacific Islander American Health Forum
Asian Pacific American Legal Center
Asian Pacific Community Fund
Asian Pacific Environmental Network
National Asian American Telecommunications Association
National Asian Pacific American Legal Consortium
National Asian Pacific Publishers Association
On Lok, Inc.
Organization of Chinese Americans
Refugee Resource Center
Self-Help for the Elderly
Southeast Asian Community Center
UCLA Asian American Studies Center
Union of Pan Asian Communities

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

CALIFORNIA/NEVADA COMMUNITY ACTION ASSOCIATION

By: /s/ Henry Knawls Date: 6/14/99
Henry Knawls
President

On behalf of itself and the following organizations:

City of Oakland/Life Enrichment Agency—Department on Aging, Health and Human Services
Amandor/Tuolumne Community Action Agency
Community Action Agency of Buttee County, Inc.
Calaveras-Mariposa Community Action Agency
Colusa-Glenn-Trinity Community Action Agency
Contra Costa County Community Services Department
El Dorado County Dept. of Community Services
Fresno County Economic Opportunities Commission
Redwood Community Action Agency (Eureka)
Northern California Indian Development Council
Campesinos Unidos, Inc.
Inyo-Mono Advocates for Community Action, Inc.
Kern County Economic Opportunity Corp.
Kings Community action Organization, Inc.
Lake County Community Action Agency
North Coast Energy Services
Lassen-Plumas-Sierra Community Action Agency
City of Los Angeles Community Development Department—Human Services & Neighborhood Development Division
Foothill Area Community Services, Inc.
Long Beach Community Services Development Corp.
Los Angeles County Department of Community & Senior Services
Jobs for Progress, Inc./SER South Bay
LA Works
Pacific Asian Consortium in Employment
Veterans in Community Service
Madera County Action Committee, Inc.
Community Action Marin

North Coast Opportunities, Inc.
Merced County Community Action Agency
Modoc-Siskiyou Community Action Agency
Monterey County Dept. of Social Services—Office For Aging and Adult Services
Napa County Council for Economic Opportunity
Nevada County Department of Housing/Community Ser
Orange County Community Development Council, Inc.
Placer County Community Services
Project GO
Riverside County Department of Community Action
Community Resource Project, Inc.
Rural Community Assistance Corp.
San Benito County Community Services and Work Force Development
Community Services Dept. of San Bernardino County
MAAC Project
Economic Opportunity Council of San Francisco
Community Design Center
San Joaquin County Department of Aging/Community Ser
Economic Opportunity Commission of San Luis Obispo
Community Action Agency of San Mateo County
Community Action Commission of Santa Barbara
Community Action Board of Santa Cruz County
Shasta Community Action Agency
Self-Help Home Improvement Project, Inc.
Solano County Community Action Agency
Sonoma County People for Economic Opportunity
Sutter County Community Action Agency
Community Action Agency of Tehama
Community Services and Employment Training, Inc.
Ventura County Commission on Human Concerns/Comm Dev
Yolo County Community Partnership Agency
Yuba County Community Services Commission
Association of Southern California Environmental & Energy Providers

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

COMMUNITY TECHNOLOGY POLICY COUNCIL

By: /s/ Deborah F. Ching Date: 6/16/99
Deborah F. Ching
Co-Chair

By: /s/ Bong Hwan Kim Date: 6/16/99
Bong Hwan Kim
Co-Chair

On behalf of itself and the following organizations:

Deborah F. Ching, Chinatown Service Center
Anni Chung, Self Help for the Elderly
Tessie Guillermo, Asian & Pacific Islander Health Forum
Margaret Iwanaga-Penrose, Union of Pan Asian Communities
Bong Hwan Kim, MultiCultural Collaborative
Gina Lew, Leadership Education for Asian Pacifics
Michael Woo, Local Initiative Support Corporation

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

HISPANIC ASSOCIATION ON CORPORATE RESPONSIBILITY

By: /s/ Jess Haro Date: 6/16/99
Jess Haro
California Chair

On behalf of itself and the following organizations:

American G.I. Forum
California Hispanic Chambers of Commerce
California Latino Civil Rights Network
Cuban American National Council
Federation of Employed Latin American Descendents
Hispanic Association on Corporate Responsibility
HOPE, A California Latina Political Organization
Latin Business Association
League of United Latin American Citizens
MANA, a National Latina Organization
Mexican American Political Association
National Hispanic Employee Association
San Diego Urban Corps
Western Region Puerto Rican Council

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

UNIVERSAL SERVICE ALLIANCE

By: /s/ Jacquelyn Brand
Jacquelyn Brand
Coordinator

Date: 6/16/99

On behalf of itself and the following organizations:

Access to Software for All People
Advocates for Consumer Equity
Alliance for Public Technology
Alliance for Technology Access
California Latino Civil Rights Network
Center for Accessible Technology
The Children's Collective, Inc.
Computer Access Center
Consumers First
MAAC Project
Radio Bilingue
San Diego Urban League
World Institute on Disability
Cheri Bryant (ACLU, Northern California)
Susan Estrada (The Internet Society)
J Craig Fong
Dr. Barbara O'Connor (Department of Communications, CSU Sacramento)
Toby Rothschild (Legal Aid Foundation of Long Beach)

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

WORLD INSTITUTE ON DISABILITY

By: /s/ Betsy Bayha Date: 6/17/99
Betsy Bayha

On behalf of itself and the following organizations:

Arkenstone
Computer Technologies Program
Smith Kettlewell Eye Research Institute
United Cerebral Palsy Golden Gate
World Institute on Disability

COUNTERPART SIGNATURE PAGE TO
GTE/BELL ATLANTIC COMMUNITY COLLABORATIVE AGREEMENT

SO AGREED:

LOS ANGELES URBAN LEAGUE

By: /s/ John Mack
John Mack
President

Date: 7/7/99

(END OF ATTACHMENT C)

ATTACHMENT D

ADDITIONAL SERVICE QUALITY REPORTS

In addition to any and all other reports now provided to the Commission, applicants shall provide the following service quality reports regarding the service quality of GTE California, or any successor utility. Each report shall be provided annually, except the Customer Calls/Complaints report, which shall be provided quarterly. Management shall attest that the information contained in each report is true and correct.[1] The reports will begin with 1999, and continue for four years after the merger is approved.[2] The reports shall be provided on compact disk media within 60 days after the end of each quarter or year.[3] One copy of each report shall be served on the Director of the Office of Ratepayer Advocates, and one copy on the Director of the Telecommunications Division, with as many other additional copies as each Director may reasonably request, along with printed copies if requested.

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[1] Applicants shall verify each report. (Rules 2.4 and 88 of the Commission's Rules of Practice and Procedure.)

[2] Exhibit 37, page 21, line 21; Exhibit 171, page 1. Merger approval is understood here to mean consummation. If, for example, the merger is consummated on April 1, 2000 reports shall be filed with data for 1999 and 2000, plus four years after merger approval, or 2001, 2002, 2003 and 2004.

[3] The report with data for 1999 shall be filed within 60 days of the date the merger is consummated. Assuming the merger is consummated by December 31, 2000, the report with data for 2000 shall be filed by March 1, 2001. Subsequent reports shall be filed by March 1 of each year. It is reasonable that the Customer Calls/Complaints report shall be provided within 60 days of the end of each quarter, beginning 60 days after the date the merger is consummated. If the merger is consummated on April 1, 2000, for example, the report for the quarters ending in 1999 and through March 31, 2000 shall be filed by May 30, 2000. If the merger is consummated on April 1, 2000, the last quarterly report shall be filed within 60 days of the quarter ending March 31, 2004.

1. Trouble Reports

   Applicants shall provide a list of all out-of-service trouble reports for residential subscribers, and a separate list for business subscribers. These lists shall include at least the following information: the month and year of the report; the account number; the wire center code associated with the account; the date reported; the date fixed; and whether the problem was referred to cable maintenance. This same data is reported in the Automated Reporting Management Information System (ARMIS) reports provided to the Federal Communications Commission (FCC) on an aggregated total company basis.

2. Non-Out-of-Service Trouble Reports

   Applicants shall provide lists of all non-out-of-service trouble reports separately for both residential and business service. These lists shall contain at least the same information as the Trouble Reports. (See Item 1 above). This same data is reported in the ARMIS reports to the FCC on an aggregated total company basis.

3. Installation Reports

   Applicants shall provide a list of installations for all residential service, and a separate list for all single-line business service. These lists shall include at least the following information: the month and year of the report; the account number, the wire center code associated with the account; the date of the order; the date of commitment; the date the installation was completed; and whether it was referred to cable maintenance because of a no-facilities condition.

4. Commitment Reports

   Applicants shall report how many commitments for installations were made and how many were missed. These lists shall be on a central-office basis, as well as on a California company-wide basis. This same data is reported in the ARMIS report on an aggregated total company basis.

5. Repair Complaint Reports

   Applicants shall provide a list of all repair complaints. This list shall include at least the following information: the date of the complaint; the account number, the wire center code associated with the account number, and the nature of the complaint.

6. Installation Complaint Reports:

   Applicants shall provide a list of all installation complaints. This list shall include at least the following information: the date of the complaint; the account number, the wire center code associated with the account number, and the nature of the complaint.

7. Operator Response Time Reports:

   Applicants shall report the monthly average speed of answers of calls to the local exchange carrier's directory assistance, repair, business office and operator services, measured from the point a call is directed to a live agent.

8. Total Number of Customer Calls/Complaints:

   Applicants shall report data on the total number of California customer calls/complaints to GTE's Action Line, GTE's Executive Office, the California Public Utilities Commission, the FCC, the Better Business Bureau and the Attorney General. These reports shall be provided on a quarterly basis showing monthly data.

(END OF ATTACHMENT D)