

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: May 17, 2005**

REGULAR _____ **CONSENT** X **EFFECTIVE DATE** _____ Upon Approval

DATE: May 6, 2005

TO: Public Utility Commission

FROM: Jim Stanage

THROUGH: Lee Sparling through Phil Nyegaard through Lance Ball

SUBJECT: VERIZON NORTHWEST, INC.: (Advice No. SC01-05) Makes special contract arrangements between Verizon Northwest Inc and a confidential customer for SONET Service.

STAFF RECOMMENDATION:

I recommend that the Commission take no action. If the Commission does not act at the end of the ninety-day expiration period, the contract is deemed approved.

DISCUSSION:

Verizon Northwest, Inc. (Verizon) filed this special contract on March 10, 2005. The purpose of the filing is to seek approval of a thirty-six month special contract with a confidential customer for Optical Carrier 192 Synchronous Optical NETWORK (OC-192 SONET) Service. OC-192 SONET is a special private line service. Verizon has asked staff not to divulge the contract customer's name. The contract filing would become effective upon Commission action and would extend for thirty-six months. Pursuant to ORS 759.250, the Commission has ninety (90) days from the date of filing to terminate the effectiveness of a special contract. For this contract that date is June 9, 2005. The contract would generate annual net revenues of approximately \$851,000, but because it is a renewal of an existing contract, the revenues do not constitute a revenue increase.

OC-192 SONET service provides 129,024 access channels for voice/data transmission at 9.953278 Gigabits per second (Gbps). OC-192 service may be used for the transmission of voice, data, and video signals, or any combination thereof. This service is provided over optical fiber facilities between two-customer designated premises, between a customer-designated premise and a central office wire center, or between central office wire centers. OC-192 service is provided over a "self-healing" network and consists of the equivalent of 5,376 DS1s, or 192 DS3s.

DS1 (Digital Signal-Level One) service provides for the two-way transmission of 1.544 Mbps digital signals, on a point-to-point basis only. The DS1 facility includes common equipment necessary to interface each of its 24 channels into the central office (CO) switch.

DS3 (Digital Signal-Level Three) service provides a high capacity facility for the transmission of 44.736 megabits per second (Mbps) isochronous serial data with the capability to channelize up to 672 channels.

The services are being provided under the contract at the following monthly unit rates:

<u>Initial Quantity</u>	<u>Enhanced Dedicated SONET Ring (EDSR) Service Element/Item</u>	<u>Monthly Recurring Charge per Unit</u>
7	OC-192 Customer Premise Node / Per Node	\$3,500.00
1	OC-192 Central Office Node / Per Node	\$3,500.00
17 Airline Miles*	OC-192 Transport (per Airline Mile)	\$105.00
Ports – per location		
14	1 Gigabit Ethernet Port, each	\$1,950.00
0	10 Megabit Ethernet Port, each	\$450.00
0	100 Megabit Ethernet Port, each	\$924.00
Rider Charges: per circuit		
96	DS1 Rider, each	\$54.00 / Circuit
4	DS3 Rider, each	\$190.00 / Circuit
7	STS1 Rider, each	\$250.00 / Circuit
19	OC3c Rider, each	\$550.00 / Circuit
0	OC12c Rider, each	\$1,760.00 / Circuit
0	OC48c Rider, each	\$3,600.00 / Circuit

The Special Contract

This service is unique to this customer because it provides a high capacity data transmission service and Verizon does not offer an equivalent service in its current tariff. Customer is currently receiving similar service under a prior agreement fully executed on March 9, 2001, and filed with the Commission as SC02-01 for which facilities will be

* Airline Miles are an estimate; actual mileage may vary. Customer will be charged actual Airline Miles.

utilized for the service furnished. However, it is treated as a new contract since ORS 759.250 (7) requires that "No contract filed under subsection (2) of this section may be automatically renewed. A contract renewal shall be treated as a new contract." The existing contract was reviewed with the Commission at the July 9, 2002, public meeting. At the public meeting the Commission took no action on Advice No. SC2-02 and pursuant to ORS 759.250, since no action was taken within ninety (90) days of the filing date, the special contract was deemed approved.

The termination liability associated with this contract requires the customer to pay twenty-five percent of the monthly rate times the number of months left under the contract. This is the same termination liability condition that applies to the company's regularly tariffed services.

This service is unique to this customer because of its capacity and delivery, which give the customer greater speed, reliability, and flexibility in data transmission. Verizon had no customers for OC-192 SONET service at the time this contract was completed. Because there was no prior special contract for the same service, the company was required by the statute to file this contract with the Commission.

The special contract customer is a sophisticated telecommunications user with extensive facilities and competitive network experience. The customer has a full time telecommunications staff supervising network services and equipment provided by other vendors. If Verizon does not provide this service to meet the customer's high capacity data transmission needs, other competitors would be able to provide the service.

Staff has reviewed the company's estimated long-run, incremental cost of service (LRIC) and estimated net margin or contribution from the proposed sales under this contract. Staff's analysis indicates Verizon would receive revenues that would exceed LRIC and provide an adequate contribution for its private line service under the proposed contract. In other words, the special contract appears to be prudent in terms of revenue sufficiency.

Procedures for Reviewing Special Contracts

Telecommunications utilities are allowed under ORS 759.250 to enter into special contracts with customers without being subject to standard tariff filing procedures under ORS 759.175. In addition, special contracts are not subject to hearings (ORS 759.180) or suspension (ORS 759.185).

The requirements for Commission approval of telecommunications special contracts are outlined in ORS 759.250 as follows. First, the contract service must have limited availability, respond to unique customer requirements, or be subject to competition. Second, prices must exceed the long-run incremental cost (LRIC) of providing the service.

Telecommunications utilities are required to file special contracts no later than ninety days following the effective date of the contract. Contracts must not exceed five years.

Last, the Commission is not required to disclose the name of the contract customer without the consent of the customer and the telecommunications utility. Staff has been asked by Verizon not to reveal the contract customer's name in this memorandum.

Furthermore, the law states that the Commission shall issue an order on the filed contract within ninety days of the filing. If the Commission does not act within ninety days of the filing, the contract is deemed approved. Staff understands that if a telecommunications utility does not provide sufficient evidence to support a contract filing under ORS 759.250, then staff may recommend that the Commission reject the contract.

Classification and Unjust Discrimination Criteria

PUC Order No. 92-651, issued May 1, 1992, adopted additional procedures and guidelines for telecommunications special contract filings. The order specifies that in assessing special contracts the Commission must consider the reasonableness of the contract rates and whether the rates result in unjust discrimination. The statutes that underlie these areas of concern are ORS 759.210 (classification of service and rates) and ORS 759.260 (unjust discrimination).

Staff's contract analysis dealing with conformance to ORS 759.210 is twofold. First, staff determines if a special contract rate class is developed by the telecommunications utility for one or more of the following reasons: a) the quality of the contract service used; b) the purpose for which the contract service is used; c) whether price competition or a service alternative exists; d) the contract service being provided; e) the conditions of contract service; or f) other reasonable considerations. Second, staff determines if the special contract results in revenue sufficient to ensure just and reasonable rates for remaining customers (a "prudency review").

In assessing whether a special contract conforms to ORS 759.260, staff determines if the special contract avoids unjust discrimination. This is basically a comparative analysis that depends on a review of the existing tariff for similar or related services.

Staff Conclusions

Staff has investigated the proposed special contract. Staff concludes that the present contract for OC-192 SONET service responds to a unique customer requirement---i.e., it is different from Verizon's other services in its capacity and delivery, which give the customer greater speed, reliability, and flexibility in data transmission that are not available under tariff. Staff believes that Verizon is acting prudently by contracting with the customer in order to obtain additional revenues while providing services at rates that exceed LRIC. Based on Oregon statutory requirements and the special contract guidelines under Commission rules, staff finds that the proposed contract does not raise issues concerning the reasonableness of rates or unjust discrimination. Last, the contract service is available to other similarly situated customers of Verizon on equal terms and conditions.

PROPOSED COMMISSION MOTION:

The Commission take no action with regard to the special contract proposed in Verizon's Advice No. SC01-05. If the Commission does not act at the end of the ninety-day expiration period, the contract is deemed approved.