

**PUBLIC UTILITY COMMISSION OF OREGON  
STAFF REPORT  
PUBLIC MEETING DATE: February 21, 2006**

**REGULAR** \_\_\_\_\_ **CONSENT**  X  **EFFECTIVE DATE**  March 8, 2006

**DATE:** February 13, 2006

**TO:** Public Utility Commission

**FROM:** Jim Stanage

**THROUGH:** Lee Sparling through Phil Nyegaard through Lance Ball

**SUBJECT:** VERIZON NORTHWEST INC: (Advice No. SC05-09) Makes special contract arrangements between Verizon and a confidential customer to provide Frame Relay 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 December 8, 2005. The purpose of the filing is to seek approval of a twenty-month special contract with a confidential customer for Frame Relay Service. The Frame Relay Service that would be provided to this customer would include a high capacity data transmission service at a discount from the current tariff rate. Verizon has asked staff not to divulge the contract customer's name. 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 March 8, 2006. The contract would have annual net revenues of approximately \$768,000.

Frame Relay Service (FRS) is a "fast packet" network service that permits the two-way transmission of data at speeds from 56 Kbps to 1.544 Mbps using Permanent Virtual Circuits (PVCs). Employing digital technology, Frame Relay Service (FRS) provides high-speed access and throughput to and among Local Area Networks, as well as computers. Utilizing statistical multiplexing, FRS enables users to allocate circuit bandwidth to applications as needed, up to the maximum bandwidth purchased, rather

than assigning fixed channels to specific applications. FRS supports transmission speeds up to 1.544 Mbps.

Permanent Virtual Circuits (PVCs) are logical circuits that define a specific path for data sent by the customer to another customer location. These circuits are virtual because they are established in software tables and do not tie up capacity when not in use. This also allows multiple PVCs to be defined over a single access line, thereby providing a single access line the capability to transmit data to multiple destinations.

### The Special Contract

This service is unique to this customer because it provides larger volume discounts than its current tariff Frame Relay Service. Because there was no prior special contract for the same service that is still in force, the company was required by the statute to file this contract with the Commission.

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.

Under the contract, the Frame Relay Service is provided at rates that are discounted by ten to twenty-five percent from the regularly tariffed rates, depending on unit volume. If Verizon does not provide this service to meet the customer's 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 producing sufficient revenues.

### 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 proposed contract responds to a unique customer requirement---i.e., it is different from Verizon's other services in that it provides larger volume discounts than are otherwise available. Staff believes that Verizon is acting prudently by contracting with the customer in order to obtain revenues and receive a term commitment from the customer 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 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. SC05-09. If the Commission does not act at the end of the ninety-day expiration period, the contract is deemed approved.